OAG

OFFICE OF THE AUDITOR-GENERAL

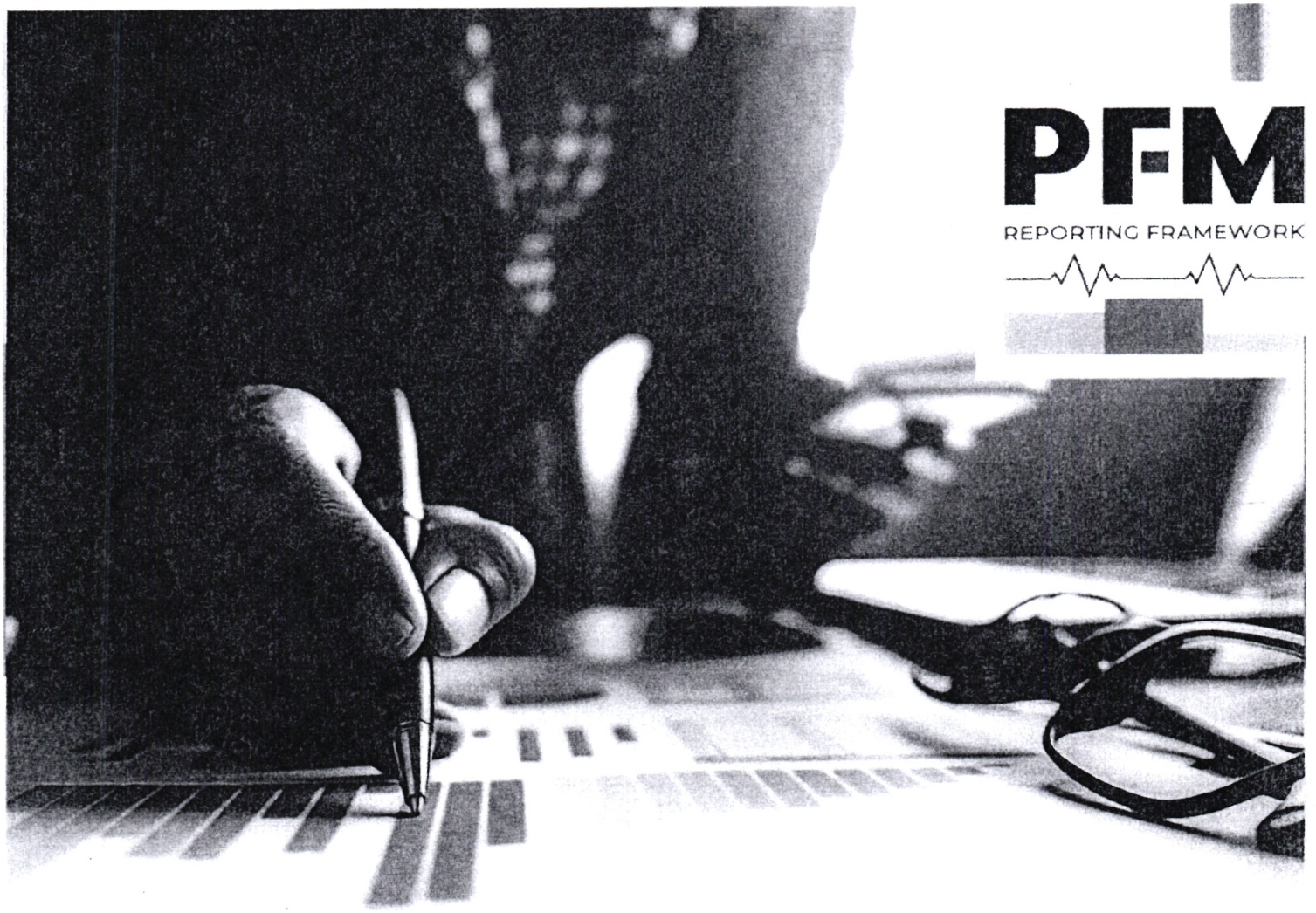
Enhancing Accountability

SPECIAL REPORT ON

PERFORMANCE OF THE

PUBLIC FINANCE MANAGEMENT SYSTEM

FOR THE YEAR 2019 - 2020



DECEMBER 2021

VISION

Making a difference in the lives and livelihoods of the Kenyan People

MISSION

Audit services that impact on effective and sustainable service delivery

CORE VALUES

Integrity

Credibility

Relevance

Accountability

Independence

MOTTO

Enhancing Accountability

FOREWORD BY THE AUDITOR-GENERAL

I am pleased to present this special audit report which assessed the performance of the Public Finance Management System for Key PFM Implementors and selected Ministries, Departments and Agencies (MDAs) involved in the implementation of the National Development Plan Vision 2030 and in particular the prioritized goals during the Financial year 2019/2020.

My Office carried out the audit under the mandate conferred to me by Article 229 of the Constitution of Kenya. The Constitution mandates the Auditor-General to audit and report within six months after the end of each financial year on the accounts of public entities, and to confirm whether or not public money has been applied lawfully and in an effective manner. Further, Section 7 Sub-section (1(a-g)) of the Public Audit Act, 2015, gives additional functions and responsibilities to the Auditor-General which include confirming whether collection of revenue and expenditure of public money has been used and applied to the purposes intended and the authority for such expenditure.

The analysis will greatly enable the various public sector institutions gauge, how well they adhere to the requirements of the Public Finance Management Act, 2012 which was enacted to provide for the effective management of public finances by both the national and county governments.

The analysis was carried out through the use of the Public Finance Management – Reporting Framework (PFM-RFTool V.2.0) developed through partnership of the African Organisation of English-speaking Supreme Audit Institutions (AFROSAI-E) (where the Office of the Auditor-General, Kenya is a member) and Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ) GmbH. The Tool enables Supreme Audit Institutions gauge the performance in the PFM cycle and analyze findings to the extent of identifying root causes of identified areas of underperformance. This in turn helps in generating appropriate audit recommendations that address the real problems as opposed to the symptoms noted.

The PFM-RF Tool also enables the analysis of performance on implementation of Sustainable Development Goals (SDGs) and disaster preparedness in our Country starting from budget preparation and approval through budget execution to accounting, reporting and oversight. The Tool supports follow up on implementation of audit recommendations of subsequent audit cycles. I am hopeful that corrective action will be taken in line with our recommendations in this report.

I wish to thank the institutions that were analyzed for the cooperation they accorded us during the exercise and wish to inform other institutions that we shall rollout the PFM-RF Tool to assess PFM performance more comprehensively for value addition in the audit process, so as to impact on service delivery and effective management of public funds in our country.

I also wish to thank the AFROSAI-E and GIZ for developing the tool that will enable us execute our mandate more effectively.

The report has been submitted to Parliament in accordance with Article 229 (7) of the Constitution. I have, as required in Section 35 of the Public Audit Act, 2015, submitted the original copy of the report to Parliament. In addition, I have submitted copies of the report to the Cabinet Secretary - The National Treasury and Planning, the Principal Secretary - The National Treasury, the Secretary - President's Delivery Unit and the Head of Public Service.

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ACRONYMS

AFROSAI-E - African Organization of Supreme Audit Institutions-English Speaking

AIA	Appropriation in Aid
BROP	Budget Review and Outlook Paper
BPS	Budget Policy Statement
CBK	Central Bank of Kenya
GDP	Gross Domestic Product
GIZ	Gesellschaft für Internationale Zusammenarbeit
IMF	International Monetary Fund
INCOSAI	International Congress of Supreme Audit Institutions
IFMIS	Integrated Financial Management Information System
ICT	Information and Communications Technologies
IT	Information Technology
KOSAP	Kenya Off-Grid Solar Access Project
KRA	Kenya Revenue Authority
LPG	Liquefied Petroleum Gas
MDAs	Ministries, Departments and Agencies
MDGs	Millennium Development Goals
MTP	Medium Term Plan
MTEF	Medium- Term Expenditure Framework
NDP	National Development Plan
NHIF	National Health Insurance Fund
PEFA	Public Expenditure and Financial Accountability
PFM	Public Financial Management
PFM-RF	Public Financial Management Reporting Framework
PPRA	Public Procurement Regulatory Authority
SAI	Supreme Audit Institutions
SAGAs	Semi-Autonomous Government Agencies
SDGs	Sustainable Development Goals
SOE	State Owned Enterprises
SRC	Salaries and Remuneration Commission
UHC	Universal Health Coverage

EXECUTIVE SUMMARY

Introduction

1. A sound PFM system is critical for service delivery. It enables a country to mobilize resources, allocate public funds, undertake public spending, account for the funds and audit and report the results. It also ensures accountability, transparency and the effective, economic and efficient collection and utilization of public resources. Thus, an efficient and effective PFM system in Kenya is a necessary condition for achieving Vision 2030, the Sustainable Development Goals, Kenya's medium-term development objectives and disaster preparedness. Though the Office of the Auditor-General audits and reports on spending in public sector institutions, it has not reported on the performance of the PFM system and its processes holistically as envisaged by the Sustainable Development Goal No. 16 which emphasizes the importance of effective and accountable institutions.
2. The PFM system in Kenya is anchored in Chapter Twelve (12) of the Constitution, the Public Finance Management Act, 2012 and the attendant Regulations of 2015. The legislative framework provides for the structure and operationalization of the PFM system. In particular, the framework identifies the core PFM institutions and their roles and also the responsibilities of individual public sector institutions and the officers in the management of public finances.
3. The assessment was motivated by the commitment of the Office to contribute to the attainment of SDGs through assessing how our PFM system supports the national development agenda, implementation of the SDGs and delivery of quality services to the people of Kenya. In addition, the COVID-19 pandemic and other disasters that Kenya has lately experienced haves necessitated the need to look at the integration of disaster preparedness in the PFM system. This looks at the ability of the country to weather the economic shocks and manage resources effectively in times of disasters. It is, therefore, necessary to establish how the PFM system is performing both holistically and at the institutional level, identify key PFM risk areas and identify the root causes for any underperformance identified.

Assessment Methodology

4. The assessment was carried out to ascertain the effectiveness of the PFM system, the underlying root causes for any underperformance and the system's disaster preparedness at two (2) levels:
   (a) core PFM institutions; and
   (b) selected Ministries, Departments and Agencies (MDAs) that are critical in the attainment of Vision 2030 and in particular the prioritized goals.
5. The core institutions are:
   (i) The National Treasury;
   (ii) Kenya Revenue Authority; and
   (iii) Parliament.
6. There were Seven (7) selected were:
   (i) Ministry of Water, Sanitation and Irrigation
   (ii) Ministry of Health
   (iii) Ministry of Agriculture
   (iv) State Department for Infrastructure
   (v) State Department for Housing and Urban Development
   (vi) Ministry of Energy
   (vii) Ministry of Education
7. The assessment covered the financial year 2019/2020 and was carried out concurrently with the financial audits. The assessment examined the performance of the PFM processes along the four (4) stages of budget cycle namely:
   (i) budget preparation;
   (ii) budget approval;
   (iii) financial management and service delivery; and
   (iv) accounting, reporting and oversight
8. The assessment also identified root causes for the underperformance based on five (5) institutional capacity areas:
   (i) policy and legal framework;
   (ii) organizational structure and human resources;
   (iii) information systems;
   (iv) governance and oversight; and

(v) communication and stakeholder management

9. Data was collected through interviews, questionnaires and document reviews. However, there was limited face-to-face interviews due to the health protocols for Covid-19.

Summary of Main Findings

(a) Weak Macroeconomic Policy, Fiscal Policy and Strategic Budgeting

10. Section 12(1)(a) of the Public Finance Management Act, 2012, requires The National Treasury to formulate, implement and monitor macro-economic policies involving expenditure and revenue.
11. The assessment identified the macroeconomic policy, fiscal policy and strategic budgeting as the weakest link in the PFM process, holistically and at institutional level. This has resulted into:
    (i) The National Treasury being unable to accurately measure economic growth rates to enable comparisons with forecasts as it does not seem to have specific economic indicators. Forecasting faces difficulties due to the COVID-19 pandemic as this had not been envisaged.
    (ii) The National Treasury provided notably higher forecasts than what was provided by the Kenya Revenue Authority, resulting to unmet revenue collection targets.
12. The root cause for the weaknesses in this process was identified as policy, legal framework and governance and oversight.

(b) The PFM process is being implemented in the institutions as required

13. The National Treasury was noted to be the weakest institution in the PFM process despite being a core PFM implementor. It scored relatively low on macroeconomic policy, fiscal policy and strategic budgeting process and financial management and service delivery areas. The National Treasury was noted to have weaknesses in procurement processes and management of cash and IFMIS among other weaknesses.
14. Among the PFM processes, the budget approval and accounting, reporting and oversight processes were found to be the most effectively implemented amongst the

institutions assessed. However, internal controls and audit were not effective as mechanisms for oversight such as audit committees were either non-existent or were not functioning as required by law. It is worth noting that The National Treasury does not have an Audit Committee.

15. The Ministry of Health was the weakest institution in the budget preparation process. Some critical priority areas identified under the Third Medium Term Plan (2018 -2022) were not included in the budget.

(c) Root causes for the weaknesses

16. The assessment noted that the weaknesses in the PFM processes and the institutions were mainly attributable to two (2) main institutional capacity areas:
    (i) policy and legal framework
    (ii) governance and oversight
17. This is an indicator that some of the policies being implemented by the government and the enabling legal framework may be inhibiting implementation of a sound PFM system. In addition, those charged with governance and oversight responsibilities such as audit committees may not be playing their roles effectively.

(d) Kenya has integrated Sustainable Development Goals into the PFM process both at the national and institutional levels

18. The government has prioritized integration of the following SDGs; 2. Zero hunger; 3. Good health and well-being; 6. Clean water and sanitation; 7. Affordable and clean energy; 9. Industry, innovation and infrastructure and 11. Sustainable cities and communities, in the current Medium-Term Plan (MTP III) through prioritizing strategic areas for intervention under the Big Four Agenda. The SDGs have also been mainstreamed in the selected institutions programmes and priorities.
19. However, the budgets for implementing the activities for the SDGs varied. The assessment revealed that 51 out of 71 MDAs are directly or indirectly involved in the achievement of the domesticated SDGs. However, the percentage of the total government budget (Recurrent and Development) that is allocated to SDGs is 29.83%.

20. The Ministry of Water, Sanitation and Irrigation allocated 91% of its budget to programmes geared towards the achievement of targets in SDG 6 which is very commendable. However, critical ministries of Health, Education and Agriculture did not adequately budget for activities geared towards implementing the SDGs. For instance, the Ministry of Health only allocated Kshs. 11.09 billion of its total budget of Kshs. 125.64 billion or approximately 8.8% towards Universal Health Coverage which is under SDG 3.

(e) The PFM processes and Institutions do not factor disaster preparedness adequately

21. The assessment noted that disaster preparedness was not factored adequately, right from fiscal policy and strategic budgeting process. At the institutional level, most of the MDAs, including the Ministry of Agriculture which is critical in food security, did not adequately prepare on disaster mitigation or response programs. The Ministry's budget had no provision for contingencies and it does not have entity wide risk management processes and policies.
22. The government has also not created the National Disaster Management Authority to coordinate and manage responses to disaster.

Conclusions

23. From the findings of the assessment, it is evident that the core PFM institutions and selected MDAs have been performing well in implementing the PFM system. In particular, the institutions have integrated the SDGs into the system thereby enabling the government to make progress towards achieving the SDGs. Despite this, the performance of the PFM system is still faced with weaknesses and systemic issues.

24. The PFM system has critical core implementors whose roles are clearly articulated in the PFMA, 2012. However, in spite of the well-defined roles, some actors and in particular The National Treasury were assessed as the weakest link in the PFM process. In addition, some process had varying degrees of implementation within the institutions with internal controls and oversight not being effectively implemented.

25. Although the PFM system is anchored in the Constitution, the policy, legal framework, and governance and oversight were the dominant root causes for the poor performance of some of the PFM processes and institutions. This may be inhibiting implementation of a sound PFM system in the public sector entities and processes.

26. Further, as a critical enabler of implementation of the SDGs, the PFM system has integrated the SDGs both at the whole-of-government and institutional level, but, there are varying degrees of prioritization of the SDGs as evidenced by budgetary allocations towards implementation of SDGs.

27. Although the PFMA, 2012 has put in place the mechanisms for expenditure relating to disasters at the national level through the Contingencies Fund, the PFM system at the institutional level has not adequately factored disaster preparedness thereby exposing the country to socioeconomic shocks in the event of disasters as the implementers of mitigation and response activities are at the institutional level.

28. All the observed shortcomings were deemed serious and critical to the country's level of SDGs implementation and disaster preparedness. The Office of the Auditor-General emphasizes the importance of a well-functioning PFM system. It requires action and commitment not only from The National Treasury and Parliament, but also from the MDAs.

Recommendations

29. To improve the PFM system, I recommend the following:

(i) Institutions and stakeholders collaborate in ensuring that a sound PFM system is achieved.

(ii) Institutions should adhere to the Public Finance Management Act, 2012 and the PFM Regulations, 2015 to improve financial management and service delivery.

(iii) Stakeholders should consider the review of existing policies and enabling legal framework for greater impact.

(iv) Improvement in governance and oversight is critical. In particular, internal controls should be strengthened and functional audit committees be constituted especially in the core PFM implementors.

30. This assessment will be carried out periodically using the PFM-RFTool to provide meaningful recommendations to Parliament and to facilitate systemic responses to the identified root causes in the PFM system that impede implementation of the SDGs and disaster preparedness.

CPA Nancy Gathungu, CBS
AUDITOR-GENERAL

20 December, 2021

Chapter 1.0 Background to the Assessment

1.1 Introduction

The Office of the Auditor-General conducted an assessment of the PFM system in Kenya. Article 229 of the Constitution of Kenya mandates the Auditor-General to audit and report within six months after the end of each financial year on the accounts of public entities, and to confirm whether or not public money has been applied lawfully and in an effective manner. Further, Section 7 Sub-section (1(a-g)) of the Public Audit Act, 2015, gives additional functions and responsibilities to the Auditor-General which include confirming whether collection of revenue and expenditure of public money has been used and applied to the purposes intended and the authority for such expenditure.

1.2 Background of the Public Finance Management in the Country

A sound PFM system is critical for service delivery. It enables a country to mobilize resources, allocate public funds, undertake public spending, account for the funds and audit and report on the results. It also ensures accountability, transparency and the effective, economic and efficient collection and utilization of public resources. Thus, an efficient and effective PFM system in Kenya is a necessary condition for achieving Vision 2030, Sustainable Development Goals, Kenya's medium-term development objectives and disaster preparedness as well as prioritized areas.

The PFM system in Kenya is anchored in Chapter Twelve of the Constitution, the Public Finance Management Act, 2012 and the attendant Regulations of 2015. This legislative framework provides for the structure and operationalization of the PFM system. In particular, the framework identifies the core PFM institutions and their roles and also the responsibilities of individual public sector institutions and the officers involved in the management of public finances.

The Public Finance Management Act, 2012 was passed by Parliament to provide for effective management of public finances by all public sector institutions in both the national and county governments. In developing the Act, Parliament was keenly aware of

the importance of having a good PFM system in determining the success or failure of devolution. To ensure a good PFM system, two objectives were considered:

i. That the PFM system was consistent with the Constitution and in particular provided for safe-guarding autonomy in financial management at both levels of government while recognizing the distinction and inter-dependence of the two levels of government as supported by Articles 6 and 189 of the Constitution. Article 6(2) states that the governments at the national and county levels are distinct and inter-dependent and shall conduct their mutual relations on the basis of consultation and cooperation, while Article 189(1)(a) states that the government at either level shall perform its functions, and exercise its powers, in a manner that respects the functional and institutional integrity of government at the other level, and in the case of county government, within the county level.

ii. That the PFM Act is firmly anchored in Article 201 of the Constitution that deals with the principles of public finance. In particular, the Act provides for openness, accountability, public participation, equitable sharing of revenue and tax burden, promoting equitable development, promoting equitable sharing of debt burden/benefits between current and future generations, and ensuring prudent and responsible use of public resources and responsible financial management and clear fiscal reporting. Parliament also enacted the Public Finance Management Regulations 2015 for both the national and county government levels.

1.3 Motivation for the Assessment

During the 2016 International Congress of Supreme Audit Institutions (INCOSAI) in Abu Dhabi, Supreme Audit Institutions (SAIs) committed to making meaningful contributions to the SDGs through re-inventing the way PFM is audited and reported upon. In particular, SAIs felt there was need to assess how the PFM system supports implementation of the SDGs. This is because funding national programs towards the achievement of these goals will only work if PFM systems function efficiently, effectively and consistently for the benefit of the citizens of every country.

In response to the need for SAIs to contribute more to the attainment of SDGs, the English-speaking subgroup of the African Organization of Supreme Audit Institutions

(AFROSAI-E) Secretariat together with GiZ developed an auditing tool called The Public Finance Management Reporting Framework" which enables SAIs to audit core public financial management institutions such as Ministries of Finance, Revenue Authorities and Parliament, as well as selected budget spending line ministries which are critical to the achievement of SDGs, such as Health and Education.

The Office of the Auditor-General was among the first countries to pilot the tool. The first assessment using the PFM-RF Tool was carried out in July 2018 as a pilot whereby a team of OAG auditors from core PFM institutions (Parliament, The National Treasury and KRA) and selected MDAs (Ministries of Education, Transport, Health, Water and Agriculture) carried out a desktop review using available information from the audits of financial year 2015/2016. A focused pilot was subsequently carried out in March 2019 using information from the audits of financial year 2017/2018. This assessment is a culmination of training of the staff and review of data and information for the financial year 2019/2020. This motivated the Office to take the lead in assessing whether the PFM systems function efficiently, effectively and consistently for the benefit of the citizens and whether the system supports the achievement of the SDGs and the national development agenda.

In addition, the COVID-19 pandemic and other disasters that Kenya has lately experienced has necessitated the need to look at the integration of disaster preparedness in the PFM system. This is done by assessing the ability of the country to weather the economic shocks and manage resources effectively including re-prioritization in times of disasters.

Chapter 2.0 Methodology

2.1 Objective of the Assessment

The PFM assessment was carried out to ascertain the performance of the core PFM Institutions and some selected Ministries, Departments and Agencies (MDAs).

The objective of this process is twofold, namely:

a. Gather information, assess and report on the effectiveness of Public Financial Management (PFM) processes through consideration of two types of entities:
   i. The Ministries, Departments and Agencies (MDAs) of national government; and
   ii. Core PFM institutions such as The National Treasury, the Kenya Revenue Authority and Parliament.

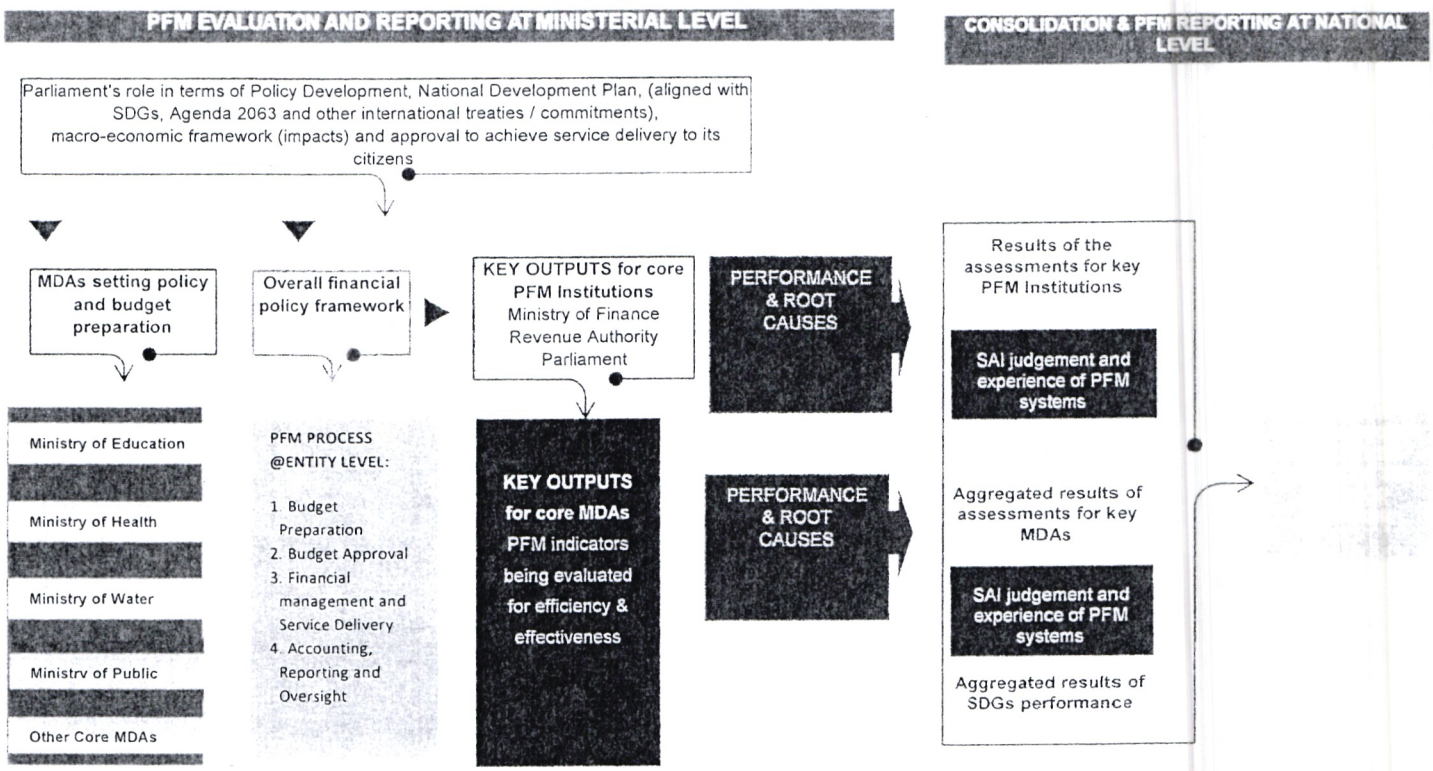
The PFM-RFTool incorporated questions that allow the assessment of compliance with sectoral SDGs from the budgeting process to accounting and reporting.

b. Consolidate findings from the individual PFM assessments conducted at MDA and core PFM institutions levels, which impact on the whole of Government's ability to:
   i. Assess the macro-economic framework, assumptions and projections used in determining the overall policy direction for achievement of the National Development Plan (NDP) Vision 2030;
   ii. Ensure alignment with UN Agenda 2030 on Sustainable Development Goals (SDGs), African Union Agenda 2063 and other international treaties and commitments; and;
   iii. Implement policy decisions.

This information will enable the Office of the Auditor-General to engage with each relevant MDA, as well as the relevant core PFM institution, on their weaknesses and developmental areas and obtain an understanding of systemic issues relating to the interactions between institutions with regard to the PFM system.

It is necessary to establish how the PFM system is performing both holistically and at the institutional level, identify key PFM risk areas and identify the root causes for any underperformance.

Figure 1: Public Finance Management Reporting Framework



Source: PFM-RF Tool

2.2 Scope of the Assessment

The assessment examined the performance of the PFM process along the four (4) stages of the budget cycle:

(i) Budget Preparation

(ii) Budget Approval

(iii) Financial Management and Service Delivery and;

(iv) Accounting, Reporting, and Oversight

The findings enable identification of the root causes of any underperformance that is based on five (5) institutional capacity areas, namely: -

(i) Policy and legal framework

(ii) Organizational structure and human resources

(iii) Information systems

(iv) Governance and oversight, and;

(v) Communication and stakeholder management

2.3 Assessment Criteria

The assessment grading ranges from zero (0) to four (4) where 0 is the worst performing grade and 4 the best performing grade. A grade of two (2) is the middle grade between the worst and best performance and therefore the risk line.

2.4 Selection of the MDAS and Core PFM Institutions

Kenya Vision 2030 was launched in 2008 as the development blueprint covering the period 2008 to 2030. Since its launch, the Vision 2030 has been implemented through the Medium-Term Plans (MTPs). We are currently in the Third Medium Term Plan (MTP III 2018 – 2022), driven by the prioritized areas of the Big Four Agenda. It is implemented on the foundations that have been put in place during the First and Second Medium Terms Plans.

The assessment selected institutions that are key to the attainment of the prioritized areas (Big Four Agenda) of:

i. Enhancing Manufacturing- 9.2.% to 20% of GDP by 2022
ii. Affordable housing-500,000 new affordable homes
iii. Universal health coverage-100% UHC by scaling up NHIF uptake
iv. Food security and Nutrition-100% food security and nutrition commitment

The institutions under review were selected from both core PFM implementers namely;

i. The National Treasury
ii. The Kenya Revenue Authority
iii. Parliament and MDAs

and the MDAs:

i. Ministry of Water, Sanitation and Irrigation
ii. Ministry of Education
iii. Ministry of Health

iv. Ministry of Agriculture
v. Ministry of Energy
vi. State Department for Infrastructure
vii. State Department for Housing and Urban Development

2.5 Methods Used in Gathering Evidence

The assessment covered the financial year 2019/2020 and was carried out concurrently with the financial audits for the same financial year. Data collection was done using both secondary and primary data. Data was collected using interviews, questionnaires and document reviews. However, only a few face-to-face interviews were carried out due to the health protocols related to the Covid-19 pandemic.

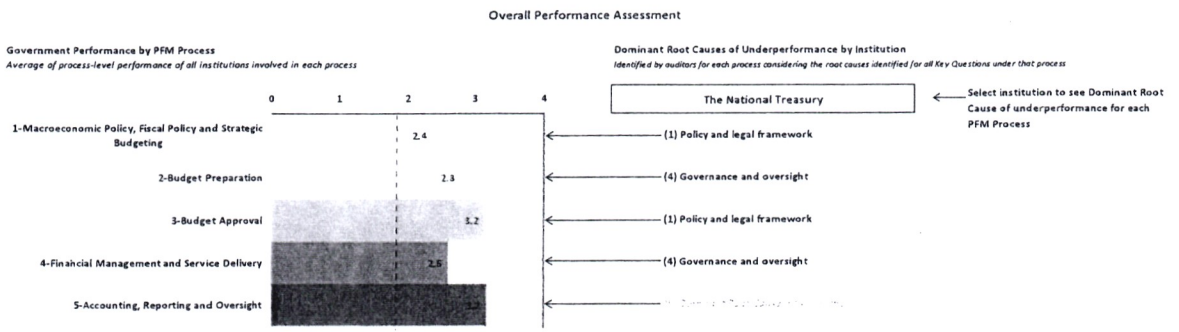
The data was analyzed using the Public Finance Management Reporting Framework (PFM-RF) assessment tool. The tool also incorporates the results of recent Public Expenditure and Financial Accountability (PEFA) assessments. Supporting documents were scanned and hyperlinked to the PFM-RF Excel based tool for cross referencing

Chapter 3.0 Detailed Results and Observations

3.1 Overall Performance by PFM Processes

Analysis of the data collected and aggregation of results provided the following conclusions as indicated in Figure 2 below.

Figure 2: Overall Government Performance by PFM Processes



Source: OAG PFM-RF Assessment Results FY 2019/2020

The Budget Approval process scored the highest at 3.2 above the risk line of 2.0. However, three of the PFM processes scored slightly above the risk line of Grade 2.0. These include:

- The Macroeconomic Policy, Fiscal Policy and Strategic Budgeting - Grade 2.4;
- Budget Preparation – Grade 2.8
- Financial Management and Service Delivery - Grade 2.6;

The macroeconomic policy, fiscal policy and strategic budgeting process scored a low grade as a result of challenges in PFM processes within The National Treasury. Section 12 (a) and (b) of the Public Finance Management Act, 2012 confers The National Treasury with the responsibility of:

(i) formulating, implementing and monitoring macro-economic policies involving expenditure and revenue;

(ii) formulating, evaluating and promoting economic and financial policies that facilitate social and economic development in conjunction with other national government entities;

The assessment noted that The National Treasury had difficulties in providing specific economic indicators due to the effects of Covid-19 pandemic in the second half of FY 2019/2020. This made it difficult for the experts to provide specific economic growth rates which could be compared with earlier forecasts.

In addition, it was noted that the Kenya Revenue Authority provided timely, accurate and evidence-based forecast to The National Treasury. However, the final forecast provided by The National Treasury including revenue targets is usually notably higher than the KRA forecast. This results into unmet revenue collection targets. As a result, the projected expenditures drive the revenue collection projections as opposed to revenue collections driving the projections of expenditures to be incurred (balanced budget).

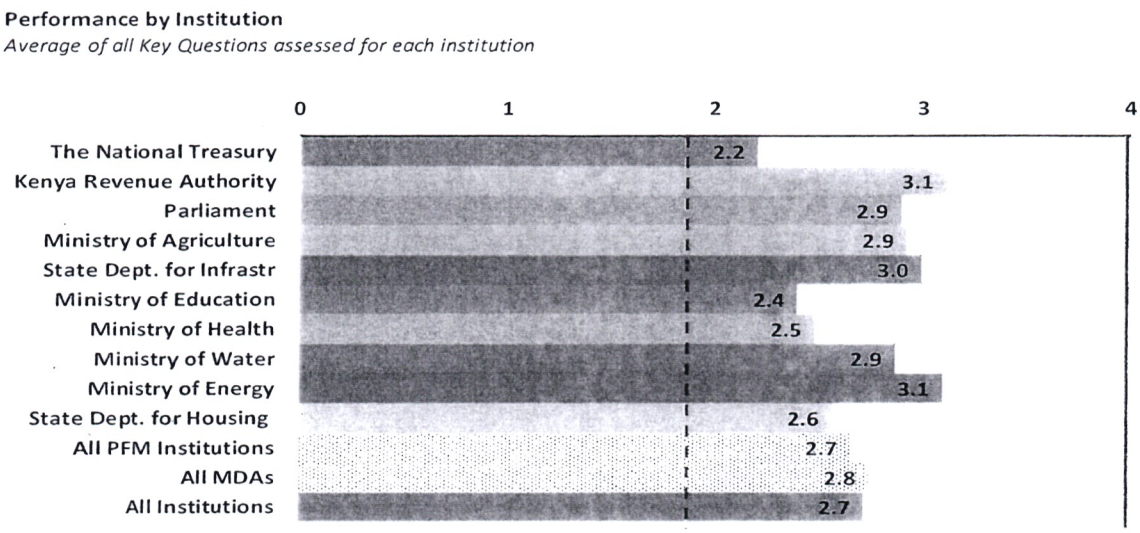
The dominant root causes for the weak forecasting and strategic budgeting processes are policy and legal framework, and governance and oversight weakness. This needs to be addressed to ensure realistic improvement in forecasting.

All institutions under review displayed weaknesses in their budgeting, financial management and service delivery processes. The grades were slightly above the risk line of 2.0 with grades of 2.6 and 2.8 respectively. Governance and oversight, and policy and legal framework are the dominant root causes for the underperformance.

3.2 Overall Performance by Institution

The overall performance per institution in the PFM Processes was also analyzed as indicated in Figure 3 below.

Figure 3: Overall Performance by institution



Source: OAG PFM-RF Assessment Results FY 2019/2020

It was noted that the best performing institutions were Kenya Revenue Authority and the Ministry of Energy as both scored a grade of 3.1. The least performing institution was The National Treasury with a Grade of 2.2. This score indicates that The National Treasury, being the key core PFM implementor has underlying weaknesses in the budget making process. It was concluded that projected expenditures drive the revenue projections as opposed to revenue collections driving the projections for budgeted expenditures (balanced budget). These weaknesses are reflected in poor performance in policy and legal framework that has implications in the implementation of the PFM processes at The National Treasury, Kenya Revenue Authority and other Ministries, Departments and Agencies.

The average score for all the institutions assessed was a Grade of 2.7 which indicates that on average Kenya is implementing the PFM processes as required. However, there is need to improve in the policy and legal framework and governance and oversight so as to enable efficient and effective implementation of the PFM processes.

3.3 Integration of Sustainable Development Goals

The Sustainable Development Goals (SDGs) were domesticated in Kenya in September 2016. Thereafter, a Country SDGs Roadmap was developed to guide the transition from Millennium Development Goals (MDGs) to SDGs. At the heart of Kenya's Vision 2030 is the mainstreaming of the SDGs at both the national and sub-national development frameworks. The principles of Kenya's National Development Agenda are aligned with the SDGs as well as the Third Medium Term Plan (MTP III 2018-2022) of Kenya Vision 2030.

In addition, all public institutions are required to mainstream the SDGs into their plans, programmes and policies and consequently report on progress of SDGs implementation as part of their performance contracting.

Figure 4: UN Sustainable Development Goals

Source: United Nations – Department of Economic and Social Affairs (Sustainable Development) https://sdgs.un.org/goals

Kenya has integrated the SDGs through prioritizing strategic areas for intervention under the Big Four Agenda. Under MTP III, the Government has prioritized the following:

i. Enhancing Manufacturing- 9.2.% to 20% of GDP by 2022

ii. Affordable housing-500,000 new affordable homes

iii. Universal health coverage-100% UHC by scaling up NHIF uptake

iv. Food security and Nutrition-100% food security and nutrition commitment

These priorities are expected to accelerate the following SDGs:

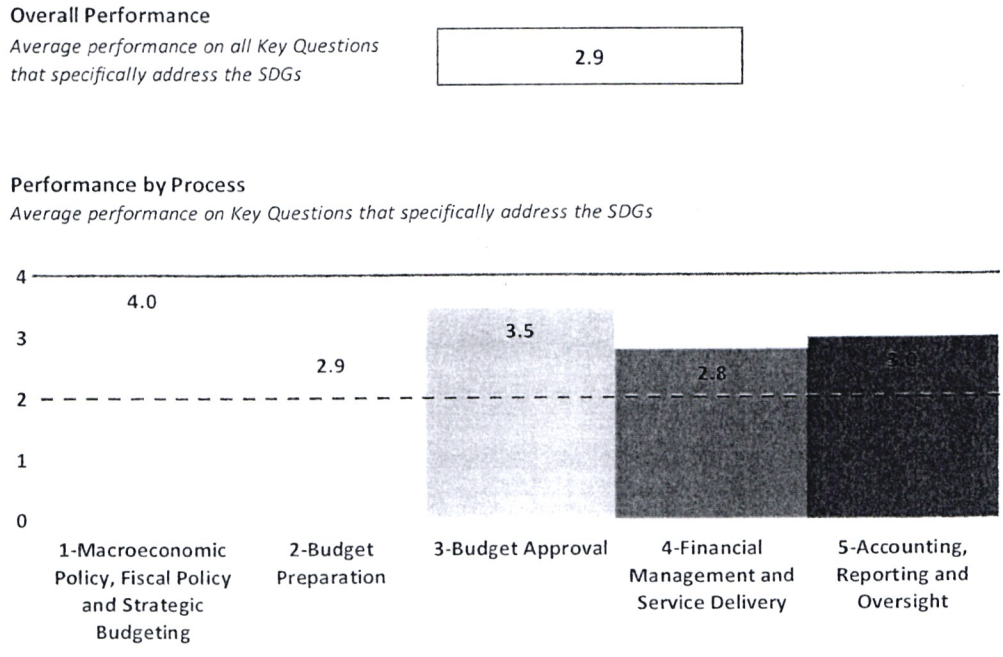
- SDG 2 - End hunger, achieve food security and improved nutrition and promote sustainable agriculture
- SDG 3 - To ensure healthy lives and promote well-being for all at all ages
- SDG 6 - Ensure availability and sustainable management of water and sanitation for all
- SDG 7 - Ensure access to affordable, reliable, sustainable and modern energy for all
- SDG 9-Build resilient infrastructure, promote inclusive and sustainable industrialization and foster innovation
- SDG 11 - Make cities and human settlements inclusive, safe, resilient and sustainable

The PFM-RF Tool incorporated questions that allow for assessment of compliance with sectoral SDGs from the budgeting process to the accounting and reporting phase. The assessment also reviewed the budgets for the core PFM institutions and the selected MDAs to determine the extent of coverage of the SDGs in the budgets.

3.3.1 SDGs Integration by PFM Processes

Kenya is integrating the SDGs in the PFM processes. However, the overall performance on SDGs for the selected institutions under review is an average score of 2.9 indicating that Kenya had not attained the highest or best grade in implementing SDGs and the various targets as indicated in Figure 5 below. This indicates the need for improvement in implementation of SDGs.

Figure 5: Integration of SDGs into PFM Processes



Source: OAG PFM-RF Assessment Results FY 2019/2020

3.3.2 Integration of SDGs by Institutions

The Medium-Term Plan (MTP) III provides the activities which the government intends to achieve in relation to the seventeen (17) SDGs which are also addressed in Vision 2030 and the prioritized areas under the Big Four Agenda. The MTP III is actualized through the Medium-Term Expenditure Framework (MTEF) which outlines the various MDAs (Sector Working Groups), either as drivers or enablers, participating in planning, budgeting and use of resources towards the achievement of the SDGs.

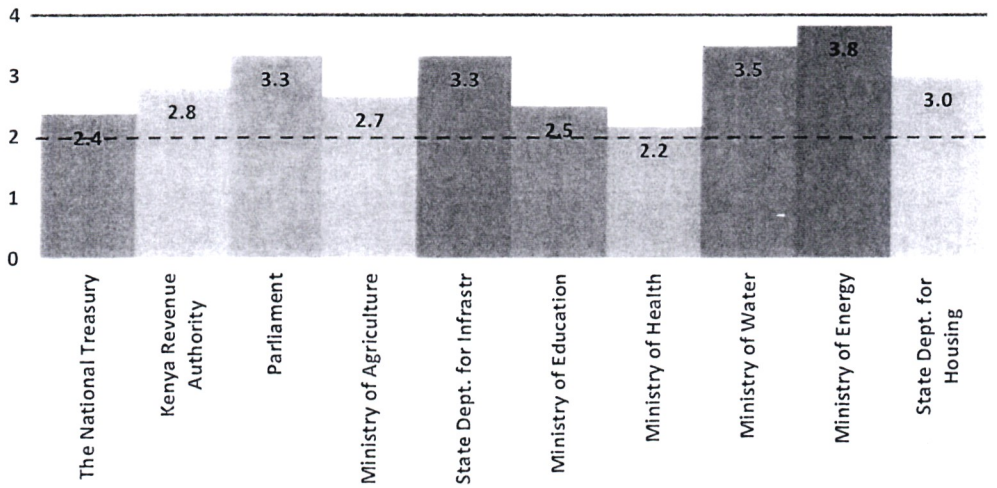
The assessment revealed that 51 out of 71 MDAs are directly or indirectly involved in the achievement of the domesticated SDGs. However, the percentage of the total Government budget (Recurrent and Development) that is allocated to SDGs is 29.83%.

The assessment indicated that the SDGs have been mainstreamed in the selected institutions' programmes and priorities. It was noted that some institutions have done well in integrating SDGs in their PFM processes as illustrated in Figure 6 below.

Figure 6: Performance of Institutions in Integrating SDGs into PFM Processes

Performance of Institutions in Integrating SDGs into PFM Processes

Average performance on Key Questions that specifically address the SDGs



Source: OAG PFM-RF Assessment Results F/Y 2019/2020

The assessment also noted that the budgetary allocation for implementing the activities for the SDGs in the core PFM institutions and selected MDAs varied as detailed below:

a) The Ministry of Energy was the best performing institution on integration of SDGs with a score of 3.8. The Ministry has integrated SDG 7 on affordable and clean energy into their PFM Processes through the sectoral budget. Domestication has been done and responsibilities allocated. From the approved budget, it was noted that the Ministry allocated Kshs.61,332,103,936 or approximately 99% out of the total budget of Kshs.61,906,101,569 to the domesticated SDGs programmes.

   The SDG integration in the Ministry is reflected in the budget proposal and the following projects which were planned for in the financial year 2019/2020:

   i) Kenya Off-Grid Solar Access Project (KOSAP) aimed at providing electricity to parts of the country that are not served by the national grid hence accelerating universal connectivity;

   ii) Last Mile Connectivity Project aimed at ensuring increased electricity access to Kenyans;

iii) Mwananchi Gas Project (Gas Yetu), aimed at increasing affordability of LPG cylinders to poor households;

iv) Street lighting in major towns to improve road and personal safety and security;

v) Hydro Dams water catchment re-afforestation; and

vi) Energy Act 2019, which has transformed the sector.

b) The Ministry of Water, Sanitation and Irrigation scored a grade of 3.5. The development budget for the Ministry was allocated to programs geared towards the achievements of targets for SDG 6 on clean water and sanitation. The development budget was Kshs.55,350,538,995 representing 91% of the total budget for the MDA.

c) The institutions that scored the lowest in integration of the SDGs include:

- Kenya Revenue Authority Grade 2.8
- Ministry of Agriculture Grade 2.7
- Ministry of Education Grade 2.5
- The National Treasury Grade 2.4
- Ministry of Health Grade 2.2

d) The Ministry of Health was the least performing institution in terms of integration and implementation of SDGs with a score of 2.2. It was assessed that the Ministry has no uptake of SDGs in national planning documents. This is further evidenced by the low score of 1.9 within the budgeting process at the Ministry of Health as illustrated in Figure 7.

The Ministry only allocated Ksh.11,093,500,000 or approximately 8.8%, out of a total initial budget of Kshs.125,644,729,264, towards Universal Health Coverage (UHC). The Kenya Health Sector Strategic Plan (July 2018 - June 2023) aims at achieving Universal Health Coverage by 2022 and ensure that the strategic direction aligns itself to the Kenya Health Policy (2014-2030). In addition, the

Strategic Plan addresses interrelations between health-related SDGs and targets, the Constitution of Kenya and Vision 2030. Target 3.8 under SDG 3 spells out the need to achieve Universal Health Coverage, including financial risk protection, access to quality essential health services, medicines and vaccines for all.

The assessment noted that the Ministry was still in the roll-out phase of the UHC and structures were not fully established. The Medical Tourism Programme was also not budgeted for despite being included in the Third Medium Term Plan 2018-2022.

The assessment results also indicate that there is very low health insurance coverage in the country. Although the National Hospital Insurance Fund (NHIF) had registered 22 million persons (beneficiaries and dependents) as at 30 June, 2020, only 3.26 million persons are covered or were active (2.0 million in the formal sector and 1.26 million in the informal sector). The government had projected to cover 12 million from the informal sector in the Medium-Term Plan 2018-2022 indicating a shortfall of 10.8 million persons.

The identified dominant root causes of underperformance in this area was governance and oversight, and policy and legal framework which affects the implementation of the SDG 3.

e) The National Treasury being a core PFM implementor and monitoring function, scored 2.4 as the average performance on SDGs. At the National Treasury level, there is no overall SDG performance monitoring taking place despite The National Treasury and the State Department for Planning being required to regularly monitor and review overall performance against SDG targets and to also provide appropriate corrective action. Information on the performance of the SDG targets by MDAs is not readily available at The National Treasury as there is no centralized way of reporting on performance other than the individual MDAs reporting independently. There is no clear policy to guide the reporting on performance in implementation of SDGs.

f) The Kenya Revenue Authority scored 2.8 as average performance on SDGs. The Revenue Authority captures the sectoral SDGs in its Corporate Plan and budget. SDGs reflected in the budget include; SDG 8 - Decent work and economic growth, SDG 9 - Industrial renovation and infrastructure, SDG 10 - Reduce inequality, SDG 16 - Peace, justice and strong institutions and SDG 17 - Partnership for the goals.

g) The target grade of 4.0 was, however, not attained by the institutions under review, indicating that there is need for improvement by all institutions in domestication, planning, budgeting, implementation and monitoring of the SDGs.

3.4 Key Overall Risk Areas

The overall risk areas identified in the assessment were macroeconomic policy, fiscal policy and strategic budgeting in The National Treasury with a score of 1.8 and the Ministry of Health budget preparation process with a score of 1.9, as illustrated in Figure 7 below.

Figure 7: Key Overall Risk Areas

Key Overall Risk Areas

Performance grade below 2 indicates risk area (shaded in red)

	National Treasury	Revenue Authority	Parliament	All PFM Institutions	Ministry of Agriculture	State Dept. for Infrastr	Ministry of Education	Ministry of Health	Ministry of Water	Ministry of Energy	State Dept. for Housing	All Ad DAs	All Institutions
1-Macroeconomic Policy, Fiscal Policy and Strategic Budgeting	1.8	3.0	N/A	2.4	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	2.4
2-Budget Preparation	2.5	2.9	N/A	2.7	2.8	3.0	2.1	1.9	3.3	3.7	3.0	2.8	2.8
3-Budget Approval	2.5	3.0	3.0	2.8	2.3	3.5	3.0	3.3	3.5	3.5	4.0	3.3	3.2
4-Financial Management and Service Delivery	2.0	3.1	N/A	2.5	3.0	2.9	2.4	2.6	2.4	2.8	2.2	2.6	2.6
5-Accounting, Reporting and Oversight	3.2	4.0	2.8	3.3	3.3	3.0	2.5	2.5	4.0	3.3	3.3	3.1	3.2

Source: OAG PFM-RF Assessment Results FY 2019/2020

3.5 Performance of Individual Institutions in PFM Processes

3.5.1 Macro-Economic Policy, Fiscal Policy and Strategic Budgeting PFM process

Macroeconomic forecasts and fiscal policies are essential components in ensuring fiscal discipline. They provide the basis for decisions on the level and composition of revenue and expenditure needed to achieve the government's fiscal objectives, and are the first steps in making choices about how the required revenues should be obtained and how

expenditure priorities can be managed within the limits that are imposed by the fiscal responsibility principles. Macroeconomic forecasts must include key macroeconomic indicators such as estimates of GDP growth, inflation, interest rates, and the exchange rate.

Kenya Revenue Authority was noted to be the strongest institution with a score of 3.0 while The National Treasury scored as the weakest with a score of 1.8 as illustrated in **Appendix 2.** The average score for the two core institutions was 2.4.

Weakness were noted in The National Treasury's report on macro-fiscal forecasts for the FY 2019/2020, where different sets of documents such as Budget Review and Outlook Paper (BROP) 2019, BROP 2020, Budget Policy Statement (BPS) 2020, BPS 2021 and the World Bank's Kenya Economic Update of November 2020 (Edition No. 22) gave different economic growth data forecasts and outturn. The actual economic growth for FY 2019/2020 could not be derived from any of those reports. This is because in the second half of FY 2019/2020 there was serious challenges faced with the economic indicators which made it difficult for the experts to provide specific economic growth rates which could be compared with earlier forecasts. The challenges came from the economic shocks experienced in the first half of the FY 2019/2020 due to the Covid-19 pandemic.

3.5.2 The Budget Preparation Process

This area of assessment considered The National Treasury, Kenya Revenue Authority and the MDAs. The Ministry of Energy was evaluated as the strongest institution with a score of 3.7 and the weakest was the Ministry of Health with a score of 1.9. The average score for all the institutions considered was 2.8 as illustrated in **Appendix 3**.

In the Ministry of Health, it was noted that the Medical Tourism Programme was not budgeted for despite being included in Clause 5.13 of the Third Medium Term Plan 2018-2022, indicating that it was not considered a high priority. Policy and legal framework was cited as the root cause of the underperformance.

In addition, there was low health insurance coverage in the country. Even though NHIF had registered 22 million persons (beneficiaries and dependants) as at 30 June 2020, only 3.26 million persons are covered/active (2.0 million formal sector and 1.26 million informal sector). The Ministry had in the Medium-Term Plan 2018-2022 projected to cover 12 million from the informal sector indicating that the government had not covered approximately 10.8 million persons as projected. The reason cited for the low health insurance coverage in the informal sector was inadequate resource allocation to NHIF to cover the informal sector since it was not prioritized and hence was not incorporated in the budget. The overall root cause of this underperformance was identified as governance and oversight.

Moreover, there was deviation between the approved budget and the actual expenditure with budget utilization being 89% of the approved budget. This was due to unrealized Appropriations-In-Aid (AIA) component of the donor funds and unrealized revenue reported by Semi-Autonomous Government Agencies (SAGAs) due to under collection of receipts, leading to failure to achieve the projected targets. Policy and legal framework were cited as the root cause of the underperformance.

3.5.3 The Budget Approval Process

This area of assessment considered Parliament, The National Treasury, the Kenya Revenue Authority and the MDAs. The State Department of Housing was assessed as the strongest institution with a score of 4.0 and the weakest was the Ministry of Agriculture with a score of 2.3. The average score of all the institutions considered was 3.2 as indicated in **Appendix 4**.

The budget for the Ministry of Agriculture was found to have no provision for unexpected events. This is due to lack of information and communication from relevant personnel on assessment of unexpected events. Policy and legal framework was cited to be the dominant root cause.

3.5.4 Financial Management and Service Delivery Process

This area of assessment considered The National Treasury, the Kenya Revenue Authority and the MDAs. Kenya Revenue Authority was identified as the strongest institution with a score of 3.1 and the weakest was The National Treasury with a score of 2.0. The average score of all the institutions considered was 2.6 as indicated in **Appendix 5**. The major contributor to the low score by The National Treasury is weaknesses in procurement processes, payroll management, poor disaster recovery procedures for IFMIS, weak cash management, weak internal controls and lack of clear updates and follow ups on implementation of the domesticated SDGs. Governance and oversight was cited to be the dominant root cause.

3.5.5 Accounting, Reporting and Oversight Process

This area of assessment considered The National Treasury, Kenya Revenue Authority and the MDAs. Kenya Revenue Authority scored as the strongest institution with a score of 4.0 and the weakest was the Ministry of Education with a score of 2.5. The average score of all the institutions considered was 3.2 as indicated in **Appendix 13**. The Ministry of Education had inadequate disclosures of contingent liabilities such as legal suits in the MDA's reporting framework, citing deficiencies in the design of the reporting framework.

It was also noted that although there are laws and regulations guiding the procurement processes of all government entities, irregularities in procurement is still an issue. Value for money concerns, irregular extension of contracts and unsatisfactory performance of contracts at The National Treasury for the FY 2019/2020 were also noted. This was due to lack of adherence to the set legal framework and regulations as well as The National Treasury not having in place an Internal Audit Committee for effective oversight.

3.6 Performance of Institutions by PFM Sub-Processes

3.6.1 Fiscal Governance

The National Treasury performed relatively well in terms of macroeconomic policy, fiscal policy and strategic budgeting by scoring a Grade between 2 and 3 in ensuring that macro fiscal forecasting and analysis were accurate, well-coordinated and integrated with

Medium Term Expenditure Framework (MTEF) as illustrated in **Appendix 1**. It is also worth noting that the Kenya Revenue Authority's good score of between 3 and 4 indicates that the Kenya Revenue Authority contribution to key macro forecasting is accurate, timely and evidence based.

The National Treasury was noted to be weak in fiscal governance mechanisms for mitigating risks as it scored a Grade between 1 and 2. This is a risk indicator that fiscal governance mechanisms might not be working as intended to mitigate against risk. One of the reasons cited in the report from the Joint World Bank – IMF Debt Sustainability Analysis on Kenya of May 2020 is that the public debt level in Kenya as a percentage of GDP had risen from 50.2% in 2015 to an estimated 61.7% at the end of 2019. This was due to the need to finance the budget deficit in order to cater for the SDGs, the National Development Plan and the political development agenda of the government, without due consideration to fiscal outlook or capability in terms of financial ability. **Appendix 2** illustrates the PFM-RF results in this area.

In addition, the assessment revealed that there is no formal, detailed regular debt sustainability analysis carried out by The National Treasury. This may be due to reluctance to release data that may contradict the medium-term debt management strategy as such data may lead to withholding of financial support by development partners.

On debt management between The National Treasury and the Central Bank of Kenya, there appears to be limited information on the role of the Central Bank of Kenya (CBK) especially regarding advising the Government on foreign debt, which represents a large proportion of debt with both monetary and financial implications on the economy. This is because CBK appears to be more of an agent of the Government (Banker) and may be, to a large extent controlled or directed by The National Treasury as the government seeks to drive the development agenda.

3.6.2 Contingency Liabilities

On assessment of whether contingency liabilities are quantified and a strategy is in place to mitigate identified risks, it was noted that quantification of outstanding loans is done according to the prepared statements. However, there appears to be no strategy in place to mitigate identified risks such as on-going concern on sustainability of State-Owned Enterprises (SOE) or collapse of the SOEs. This is due to lack of a proper structure for identifying reasons for justification of loan guarantees by the government. Some SOEs are governed through political appointments and the guarantee of obligations or loans is usually without requisite data, concrete plans or turn-around strategies.

3.6.3 Budget Preparation

The core PFM institutions (The National Treasury and Kenya Revenue Authority) and the MDAs performed well on budget preparation by scoring between 2 and 3 in ensuring that the budget is prepared and organized in line with MTEF, National Development Plan, The National Treasury circulars and sector strategies as illustrated in **Appendix 3**.

3.6.4 Budget Approval

In terms of budget approval, The National Treasury performed well by scoring between 2 and 3 on submission of the budget in line with the laws and preparation of complete and comprehensive budgets including supplementary budgets. Parliament scored between 3 and 4 in ensuring that the budget is well debated, goes through the due process and is approved in accordance with the law. The National Treasury and the MDAs performed well with a score of 3 to 4 in ensuring that the approved budget is near sufficient for KRA and MDAs to deliver on core services as indicated in **Appendix 4**.

3.6.5 Financial Management and Service Delivery

On Financial Management and Service Delivery, core PFM institutions have a relatively good score of between 2 and 3 in procurement, payroll management, information system, revenue policy and management and monitoring of service delivery (**Appendix 5**).

a) Procurement Systems

In the assessment on whether procurement systems are functioning in a transparent and competitive manner including appeals, The National Treasury was noted to be risky. It was also noted that although there are laws and regulations guiding the procurement processes for all government entities, irregularities in procurement are still reported. Value for money concerns, irregular extension of contracts and unsatisfactory performance of contracts by the contractors at The National Treasury for the FY 2019/2020 were observed. This was due to lack of proper adherence to the set legal framework and regulations to guide procurement. There may be vested interests by the parties involved in the procurement process who would want to exploit the weaknesses in internal controls and oversight emanating from the lack of a vibrant Audit Committee as required by Section 73 (5) of the PFM Act, 2012 (**Appendix 6**).

It was also noted that the website of the Public Procurement Regulatory Authority (PPRA) was not updated and did not have procurement information for the year 2020. Further, for both websites of PPRA and The National Treasury, it was noted that the information contained was not complete or in accordance to Section I (C) of the Executive Order No.2 of 2018. This was occasioned by laxity on the part of PPRA officers to enforce the Executive Order No.2, 2018 either due to lack of capacity in terms of human resources or failure by the procuring entities to provide the required information on a timely basis. Information relating to award of contracts was not provided.

b) Payroll Management

The Ministry of Education and the Ministry of Health scored Zero (0) on the robustness of payroll in terms of the payroll matching the actual workforce and regular review of the integrity of the payroll (**Appendix 7**). Some members of staff in the Ministry of Education

were earning a net pay less than a 1/3 of their basic pay in contravention of Section 19(3) of the Employment Act, 2007. This is mainly caused by override of controls and lack of monitoring by the staff involved. Therefore, governance and oversight were identified as the root cause. For the Ministry of Health, it was noted that the payroll is not regularly reviewed attributing this to organization structure and weaknesses in human resources.

On the question of whether there is efficient and lawful use of temporary employees in terms of their role, remuneration and number, the Ministry of Education had a Zero (0) score. The assessment found that 3,000 temporary employees were not on the payroll and were offering voluntary services at a monthly stipend of Kshs.2,000 on a continuous basis. The data however, was not verifiable as presented. Governance and oversight was cited to be the main dominant cause.

c) Information Systems

Kenya Revenue Authority had Zero (0) score on whether KRA's IT systems effectively integrate with the government IT systems (**Appendix 8**). KRA IT systems are not integrated with Government systems because they are incompatible.

The Ministry of Health had a Zero (0) score on effective control, oversight and regular maintenance of key government IT systems. The Ministry did not have an IT Strategic Committee or an IT Strategic Plan that supports business requirements and ensures that IT spending remains within the approved IT Strategic Plan. There was no formally approved IT Security Policy to ensure data confidentiality, integrity and availability, formal, documented and tested emergency procedures, copies of the IT continuity plan or an off-site disaster recovery plan. There were no backups stored in a secure off-site location. Lack of a formal ICT Policy was attributed to governance and oversight.

The Ministry of Agriculture had Zero (0) score on availability of disaster recovery procedures. The Ministry had no adequate and approved IT policy. A draft ICT Security Policy, drafted in April, 2016 was provided. However, the document had not been exhaustively reviewed to incorporate changes in the categorization of state departments. Stakeholders initially involved in the preparation of the ICT Security Policy were Heads of

the various departments from the Ministry of Livestock, Agriculture and Fisheries who were also part of the ICT Security Committee. The changes in categorization of the Departments requires the ICT Committee to be reconstituted to accommodate other State Departments, which was yet to be done.

d) Revenue Policy and Management

On the question of whether the Kenya Revenue Authority contributed towards the tax policy development process, KRA scored Zero (0) (**Appendix 9**). Although Kenya Revenue Authority contributes towards tax development policy through the Policy Unit and the Committee of Revenue Strategy and Technology, there was no evidence provided on its contribution.

On the question on whether debtors were being monitored and followed up at the MDA level, the State Department of Housing and Urban Development scored Zero (0). In the State Department for Housing and Urban Development, individual debtors are not followed up because rent is deducted through check off system. The money owed is, therefore, not attributed to individuals but to other State Departments and County Governments that do not remit the full amounts after deductions.

A Zero (0) score was also obtained by the State Department of Housing and Urban Development and the Ministry of Energy, on whether the MDAs have in place systems, processes and procedures to manage internally generated funds. In the State Department for Housing and Urban Development, it was found that market rent rates were not updated because the State Department had not initiated the process. The market rent rates, if reviewed, are likely to be higher than the house allowances of some of the lower cadres of staff and, therefore, this has to be done in consultation with the Salaries and Remuneration Commission (SRC). This underperformance was attributed to governance and oversight as the cause of the underperformance.

In the Ministry of Energy, systems, processes and procedures on revenue had not been developed. Funds were however, released to the energy centers through the District Treasuries and all original documents were maintained at the energy centers. The reason

cited for this is that the volume of transactions was minimal and spontaneous in nature. Further, this was not a priority focus of the energy centers.

e) Cash Management

Some of the institutions performed relatively well on cash management. However, the Ministry of Education, the Ministry of Health and the Ministry of Water, Sanitation and Irrigation scored a grade of 1 (**Appendix 10**).

f) Internal Control and Audit

Assessment on availability and effectiveness of internal controls and audit revealed that The National Treasury and all MDAs had material weaknesses and risks (**Appendix 11**).

The following is an analysis of the weakness identified in each PFM implementer;

(i) The National Treasury

The National Treasury Budget is reviewed by the Cabinet after it has been submitted and any spending of funds that have not been initially appropriated are approved through supplementary appropriation. Supplementary appropriation occurs majorly due to financial shortfall to finance Government approved activities as a result of low revenue collection and poor budgeting strategy. Moreover, the current budget strategy is an expenditure-based budget which triggers revenue collection rather than identifying revenue which in turn can support the expenditure.

It is also worth noting that the Internal Audit Department gave reports on The National Treasury Fleet management but due to the non-existence of the Audit Committee, the report was not reviewed or its findings implemented. Lack of an Audit Committee is a breach of Section 73(5) of the PFM Act 2012 which requires an Audit Committee in all public sector entities.

(ii) Ministry of Agriculture

The Internal Audit Department at the State Department for Livestock carried out only one out of the ten planned audit assignments during the period under review. Further, the Internal Audit Department did not carry out audit reviews of 2019/2020 reports and

Financial Statements as provided by law that the same should be reviewed by Internal Audit Function and the Audit Committee before signing and approval of financial statements. This was attributed to lack of facilitation due to delay in disbursement of funds occasioned by competing interest across government departments.

The Ministry of Agriculture, Livestock, Agricultural Research, Fisheries and Blue Economy had constituted an Audit Committee. However, the Committee did not convene or hold regular meetings during the year as stipulated in the Public Finance Management Regulations, 2015. Lack of adequate governance and oversight is the dominant root cause for poor performance.

(iii) State Department for Infrastructure

The internal audit recommendations were partly implemented due to Covid-19 pandemic that hampered normal operations of the Department for Quarter 3 and Quarter 4 of the financial year.

It was noted that the Ministry has an Audit Committee, although the Committee had not held any meetings. This was attributed to poor remuneration and lack of funding by the Ministry since the Audit Committee is a ministerial Audit Committee and not a State Department Committee. The Ministry of Transport, Infrastructure Housing and Urban Development, and the Ministry of Public Works constituted an Audit Committee during the Financial Year 2019/2020 to offer services to the five state departments under the entire Ministry. However, some of the State Departments did not have any budget for the Audit Committee and were, therefore, unable to contribute funds to the Ministry for remuneration of the Audit Committee Members. The Covid-19 pandemic also hindered performance of the Audit Committee.

(iv) Ministry of Education

In the Ministry of Education, the Audit Committee had not been established. As a result, the internal audit reports were neither reviewed nor discussed by the Audit Committee for implementation. No reason was given for the delay in constituting an Audit Committee. Lack of governance and oversight was the root cause attributed to the poor performance.

(v) Ministry of Health

The Ministry of Health did not have an operational Audit Committee. There was lack of a substantive Chairman as the previous Chairman had resigned due to his appointment in another Audit Committee. This resulted to lack of effective oversight, follow up and implementation of internal audit recommendations.

(vi) Ministry of Water, Sanitation and Irrigation

The Internal Audit of the Ministry of Water, Sanitation and Irrigation conducted only five (5) audits out of the planned eight (8) whose recommendations were yet to be implemented. The reports did not meet the standards as outlined in Gazette Notice No. 40 of 2016 on inclusion of Management comments in the audit reports. The audit findings were discussed with Management. However, the Management did not provide any response in writing and the reports were forwarded without comments to the Accounting Officer. The Audit Committee came into effect towards the end of the financial year 2019/2020 and did not hold any meetings in the year under review. Lack of effective governance and oversight is again the dominant root cause.

(vii) Ministry of Energy

The internal audit reports of the Ministry of Energy were not subjected to review by the Audit Committee in the year under review since the Audit Committee had only been constituted in 2019/2020. Further, the Members were unable to convene due to challenges posed by COVID-19.

(viii) State Department of Housing and Urban Development

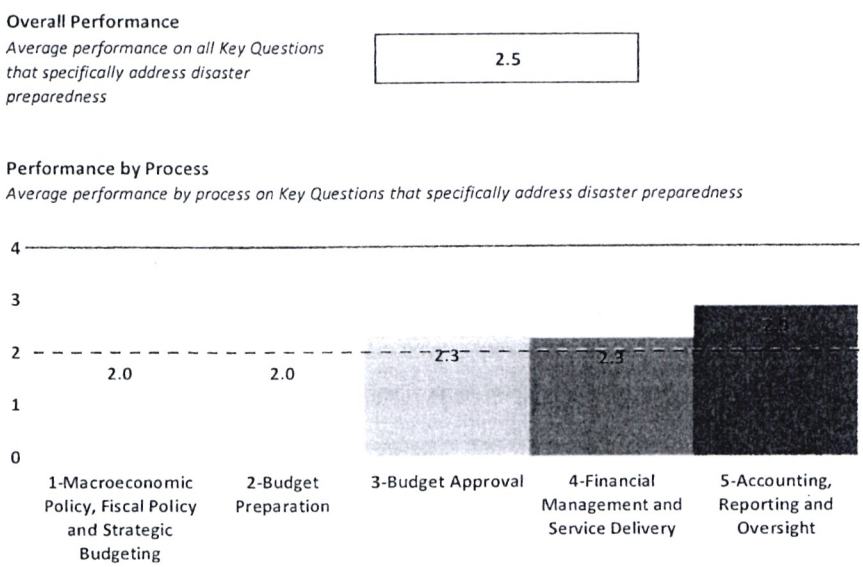
The Internal Audit Unit at the State Department for Housing and Urban Development was functional. However, the internal audit reports were submitted to the Accounting Officer without being subjected to the Audit Committee as it was not in existence. Reasons cited was that the Ministry had not identified suitable officers to serve in the Audit Committee. The Ministry advertised for the positions which were unresponsive. The allowances payable to the Audit Committee Members were deemed not attractive and therefore did not attract competent and qualified persons for the position.

3.7 Performance on Disaster Preparedness

3.7.1 Performance by PFM Processes

Disaster preparedness in Kenya has been an area of concern and this can be confirmed through the results of analysis on the overall performance in the PFM Processes (**Figure 8**).

Figure 8. Performance on Disaster Preparedness



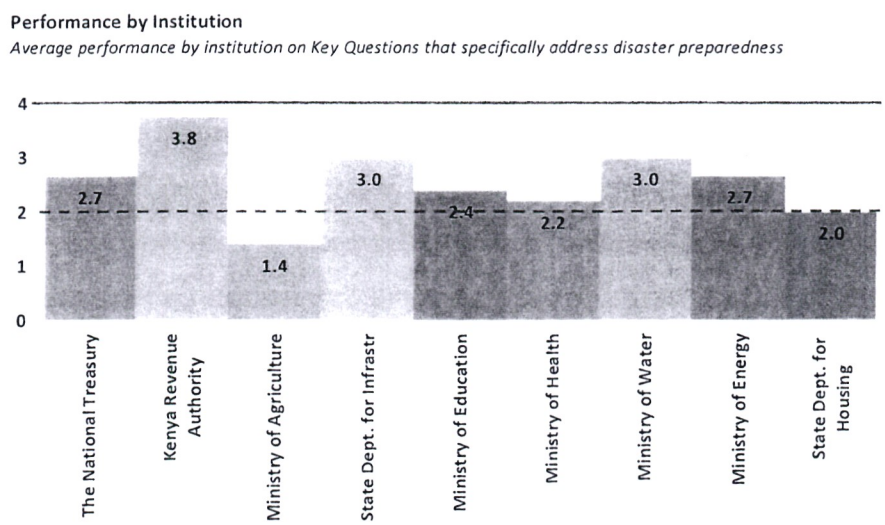
Source: OAG PFM-RF Assessment Results FY 2019/2020

The PFM Processes only scored slightly above the risk line or on the risk line of grade 2.0 as indicated below;

1. Macro-economic policy, fiscal policy and strategic budgeting – Grade 2.0
2. Budget preparation – Grade 2.0
3. Budget approval – Grade 2.3
4. Financial management and service delivery – Grade 2.3
5. Accounting, reporting and oversight – Grade 2.9

3.7.2 Performance per Institution on Disaster Preparedness

Figure 9: Performance by Institution



Source: OAG PFM-RF Assessment Results FY 2019/2020

i) The Ministry of Agriculture scored a grade of 1.4. This is a risky area and it indicates that the Ministry is not well prepared with disaster mitigation or response programs. This can be clearly supported through the effects faced by the country during perennial drought and flood seasons. The country faces difficulties in supply of food to the arid and semi-arid areas. Regulation 105(1-a-b) of the Public Finance Management (National Government) Regulations, 2015 provides that the Accounting Officer should ensure that national government entities develop risk management strategies, which include fraud prevention mechanism, systems of risk management and internal controls that builds robust business operations. In the year under review, it was noted that there was no well documented Enterprise Wide Risk Management process and policies in place to effectively guide the Ministry's risk management response or mitigation. The Ministry's budget had no provision for unexpected events or contingencies as indicated in Figure 8 above.

ii) The State Department of Housing and Urban Development scored a grade of 2.0 which lies on the risk line. It was noted that the State Department had no provision

for contingencies. In case of emergencies, the funding is done through the Contingency Fund managed at The National Treasury.

iii) The Ministry of Energy with a grade of 2.7 had integrated solutions in place for high absence of work force during disaster periods including: allocation of extra responsibilities to available workforce (acting appointments), secondment of workforce from other public institutions, extension of working hours and automation of processes. However, a Disaster Recovery Plan had not yet been developed and approved. The root cause of this underperformance was attributed to policy and legal framework.

iv) The National Treasury scored a grade of 2.4. The mechanisms to allow for emergency spending, reprioritization (reallocation of funds) and supplementary budgets to meet unforeseen demands during disaster periods are in place under the Constitution, the PFM Act, 2012 and other legislation. However, it was noted that the Contingencies Fund for Financial Year 2019/2020 did not have any expenditure in terms of disaster spending despite having a provision of Kshs.7 billion.

In addition, expenditures under Article 223 of the Constitution were noted for various MDAs and Votes which, although later ratified under subsequent supplementary budgets, did not meet the threshold for emergencies. It was also noted that after the onset of the Covid-19 pandemic, the funds set out for disaster preparedness in the Contingencies Fund were severely inadequate which led to the Government borrowing Kshs.214.9 billion to cater for the Covid-19 emergency response and to seek contributions and donations from donors, businesses and the public. Although it was noted that a proposal to create a National Disaster Management Authority whose functions were to include the coordination and control of response to, and management of disasters, the Authority had not yet been created. The root cause of underperformance was noted to be governance and oversight.

Chapter 4.0 Conclusion

From the findings of the assessment, it is evident that the core PFM institutions and selected MDAs have been performing well in implementing the PFM system. Despite this, the performance of the PFM system is still faced with systemic weaknesses and other challenges.

Among the PFM processes, the macroeconomic policy, fiscal policy and strategic budgeting was not only the weakest PFM processes from the assessment but was also one of the key risk areas both at the overall and the institutional levels. In addition, the PFM system has critical core implementors whose roles are clearly defined in the Constitution and the Public Finance Management Act, 2012. However, some actors and in particular The National Treasury were assessed as the weakest link in the PFM process. These weaknesses may have affected The National Treasury's ability to provide near realistic forecasts on economic growth. In addition, some process had varying degrees of implementation within the institutions with internal controls and oversight not being effectively implemented.

Despite the PFM system being anchored in the Constitution, the policy, legal framework, and governance and oversight were assessed as the dominant root causes for the poor performance of some of the PFM processes and institutions. This may be inhibiting implementation of a sound PFM system.

As a critical enabler of implementation of the SDGs, the PFM system has integrated the SDGs both at the whole-of-government and institutional level thereby enabling the government to make progress towards achieving the SDGs. Through the MTP III and focus on the prioritized areas under the Big Four agenda, the PFM system has prioritized six (6) critical SDGs as evidenced by the high score in macroeconomic policy, fiscal policy and strategic budgeting process on integration of SDGs. However, there were varying degrees of prioritization of the SDGs as evidenced by budgetary allocations towards implementation of SDGs. Of concern is the government budget allocation towards SDGs which was 29.8% of the total budget despite 51 out of 71 MDAs being directly of indirectly

involved in implementation of SDGs. This undermines the efforts of the government in achieving the SDGs by 2030.

Although the PFMA, 2012 has put in place the mechanisms for expenditure relating to disasters at the national level through the Contingencies Fund, the PFM system at the institutional level has not adequately factored disaster preparedness, thereby exposing the country to socio-economic shocks in the event of disasters.

All the observed shortcomings were deemed serious and affect the country's level of SDGs implementation and disaster preparedness. The Office of the Auditor-General would like to underline the importance of a well-functioning robust public finance management system. This requires action and commitment not only from Parliament and The National Treasury, but also from the Ministries, Departments and Agencies who are charged with the implementation of the PFM system, for sustainable development and delivery of quality services to the citizens.

Chapter 5.0 Recommendations

After analyzing the performance of the public finance management processes using the Public Finance Management Reporting Framework Tool for the selected institutions, it is recommended as follows;

i) Institutions and stakeholders corroborate in ensuring that a sound PFM System is achieved.

ii) Adherence to the guidelines of Public Finance Management Act, 2012 and the PFM Regulations, 2015 will greatly impact on accountable and prudent financial management and service delivery to the citizens.

iii) Realistic and timely approval of budgets will enable timely and quality service delivery and this will assist in achieving value for money from utilization of funds during each financial year.

iv) Review of some of the policies and set legal framework will assist in solving some of the problems faced in achieving a sound PFM system.

v) Improvement on governance and oversight roles by the designated stakeholders will ensure adherence to the PFM processes, implementation of the audit recommendations and follow up.

vi) Institutions should incorporate the Sustainable Development Goals Targets under their mandate and appropriate budgets to enable achievement of the various SDGs. This can be emulated from the Ministries that have successfully incorporated specific SDG Targets in the budget like the State Department of Energy.

vii) A comprehensive system for monitoring and reporting on implementation of domesticated SDGs should be developed and implemented. This will ensure that the country has data and information for use in Voluntary National Reporting (VNR) and also for adequate monitoring.

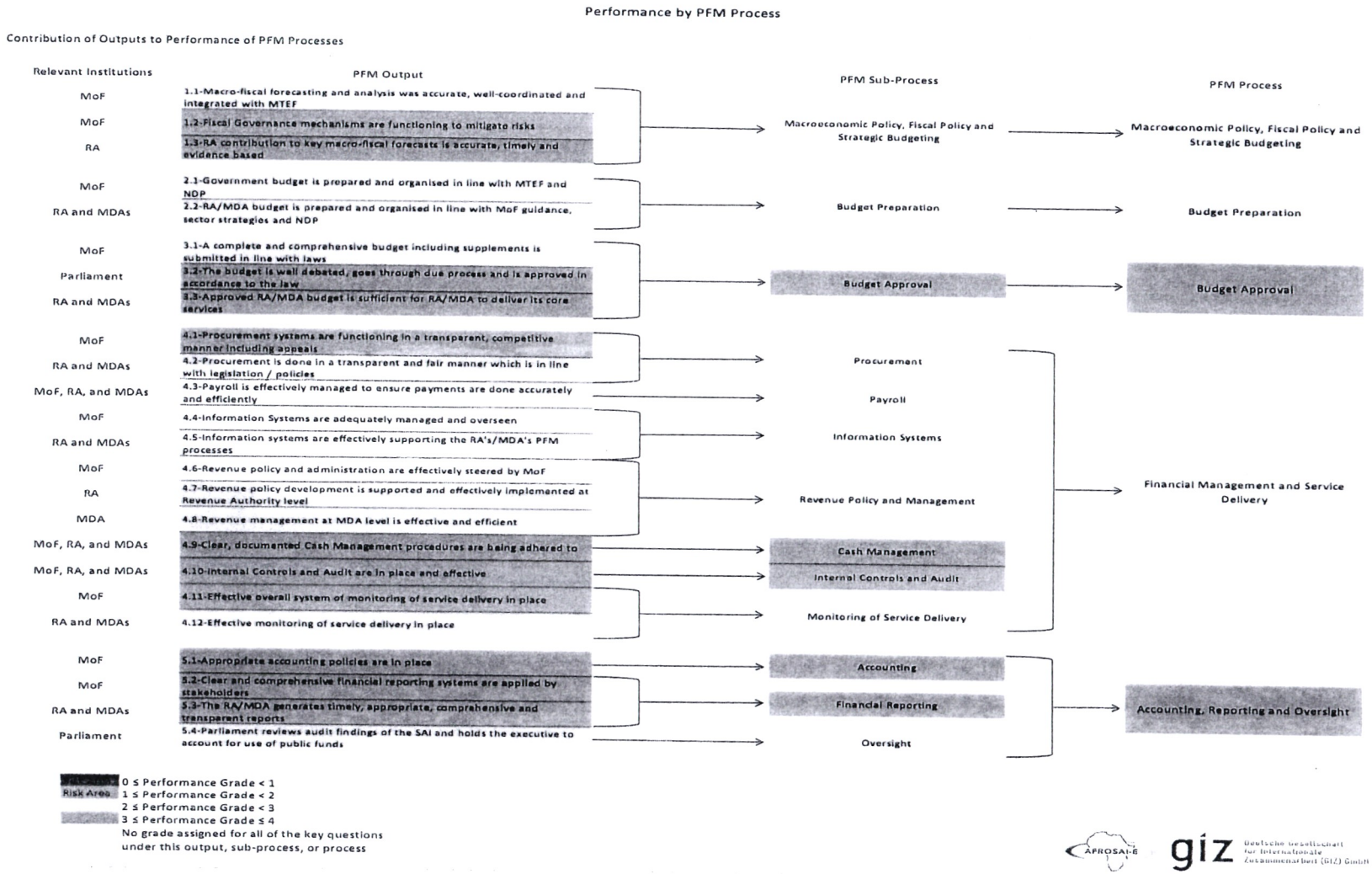
viii) Disaster and emergency preparedness should also be a key consideration in the individual ministry's budgets. It was noted that the majority of the MDAs depend on the Contingency Fund maintained at The National Treasury which was found to be not only insufficient to meet all the emergencies but required procedures to access. This curtails emergency preparedness and mitigation in a timely, efficient and effective manner by the MDAs who are the implementors.

ix) In accounting and reporting, I recommend that specific mechanisms for tracking and accounting for resources deployed for use in emergencies and transparent reporting of the same be put in place.

x) To strengthen internal controls, MDA's and core PFM implementors should constitute functional Audit Committees to improve governance and oversight of internal activities for the entities and to ensure audit recommendations from both internal and external audit are implemented.

Appendices

Appendix 1: Performance by PFM Process



Appendix 2: Performance: Macroeconomic Policy, Fiscal Policy and Strategic Budgeting

Performance: Macroeconomic Policy, Fiscal Policy and Strategic Budgeting

Overall Process Performance
Average of the performance of all the institutions engaged in this process

2.4

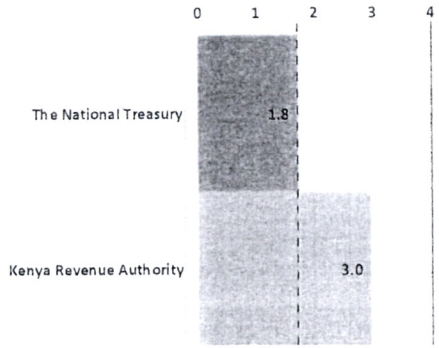
Key Risk Area?
Risk Area if the performance grade is less than 2

No

Quality Assessment
Number and percent of Key Questions with response of "Not applicable"

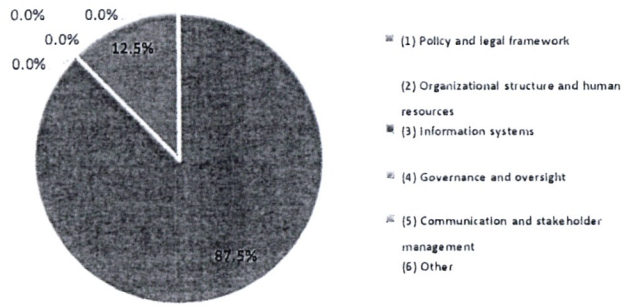
Not applicable		All others		Total questions
0	0.0%	9	100.0%	9

Performance by Institution
Average of all Key Questions assessed for this process for each institution



Risk area below this line
Target performance grade

Root Causes of Underperformance
Percent assignment of each Root Cause of Underperformance across all Key Questions for this process (excludes Key Questions with a performance grade of 4 which were not assigned a Root Cause of Underperformance)



Dominant Root Cause of Underperformance by Institution
Identified by auditors considering the root causes identified for all Key Questions under this process

The National Treasury	(1) Policy and legal framework
Kenya Revenue Authority	(4) Governance and oversight

Appendix 3: Performance: Budget Preparation

Performance: Budget Preparation

Overall Process Performance
Average of the performance of all the institutions engaged in this process

2.8

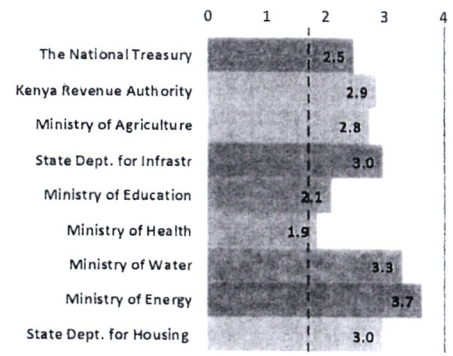
Key Risk Area?
Risk Area if the performance grade is less than 2

No

Quality Assessment
Number and percent of Key Questions with response of "Not applicable"

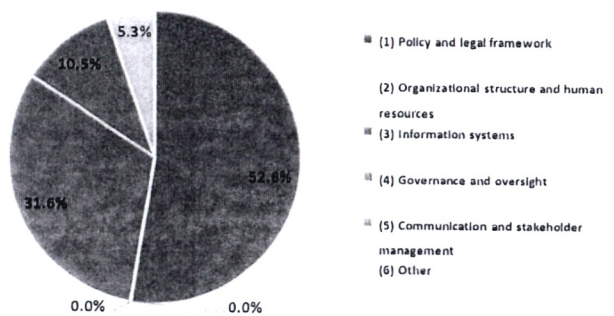
Not applicable		All others		Total questions
1	1.2%	81	98.8%	82

Performance by Institution
Average of all Key Questions assessed for this process for each institution



– – – – Risk area below this line
———— Target performance grade

Root Causes of Underperformance
Percent assignment of each Root Cause of Underperformance across all Key Questions for this process (excludes Key Questions with a performance grade of 4 which were not assigned a Root Cause of Underperformance)



Dominant Root Cause of Underperformance by Institution
Identified by auditors considering the root causes identified for all Key Questions under this process

The National Treasury	(4) Governance and oversight
Kenya Revenue Authority	(4) Governance and oversight
Ministry of Agriculture	(4) Governance and oversight
State Dept. for Infrastr	(1) Policy and legal framework
Ministry of Education	(1) Policy and legal framework
Ministry of Health	(1) Policy and legal framework
Ministry of Water	N/A
Ministry of Energy	(1) Policy and legal framework
State Dept. for Housing	

Appendix 4: Performance: Budget Approval

Performance: Budget Approval

Overall Process Performance
Average of the performance of all the institutions engaged in this process

3.2

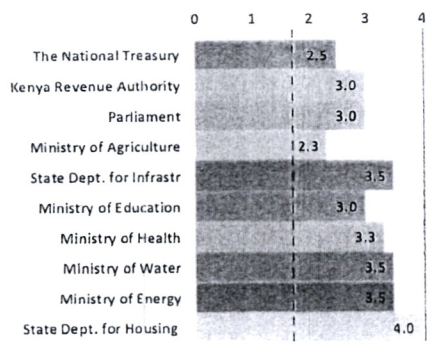
Key Risk Area?
Risk Area if the performance grade is less than 2

No

Quality Assessment
Number and percent of Key Questions with response of "Not applicable"

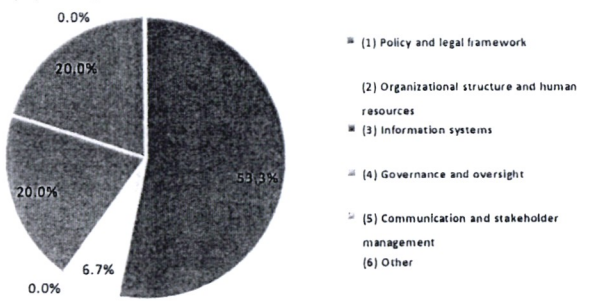
Not applicable		All others		Total questions
5	16.1%	26	83.9%	31

Performance by Institution
Average of all Key Questions assessed for this process for each institution



- - - - - Risk area below this line
——— Target performance grade

Root Causes of Underperformance
Percent assignment of each Root Cause of Underperformance across all Key Questions for this process (excludes Key Questions with a performance grade of 4 which were not assigned a Root Cause of Underperformance)



Dominant Root Cause of Underperformance by Institution
Identified by auditors considering the root causes identified for all Key Questions under this process

The National Treasury	(1) Policy and legal framework
Kenya Revenue Authority	
Parliament	(2) Organizational structure and human resources
Ministry of Agriculture	(1) Policy and legal framework
State Dept. for Infrastr	
Ministry of Education	(1) Policy and legal framework
Ministry of Health	N/A
Ministry of Water	(1) Policy and legal framework
Ministry of Energy	(1) Policy and legal framework
State Dept. for Housing	

Appendix 5: Performance: Financial Management and Service Delivery

Performance: Financial Management and Service Delivery

Overall Process Performance
Average of the performance of all the institutions engaged in this process

2.6

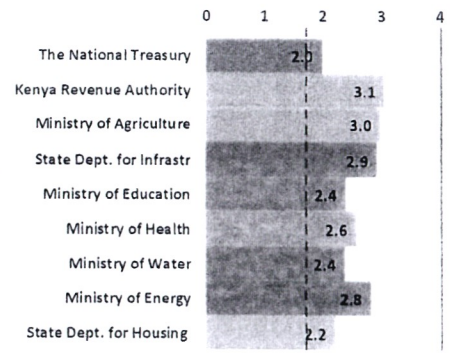
Key Risk Area?
Risk Area if the performance grade is less than 2

No

Quality Assessment
Number and percent of Key Questions with response of "Not applicable"

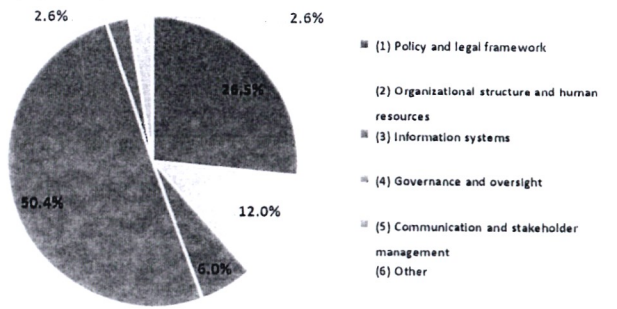
Not applicable		All others		Total questions
23	9.5%	218	90.5%	241

Performance by Institution
Average of all Key Questions assessed for this process for each institution



- - - - Risk area below this line
——— Target performance grade

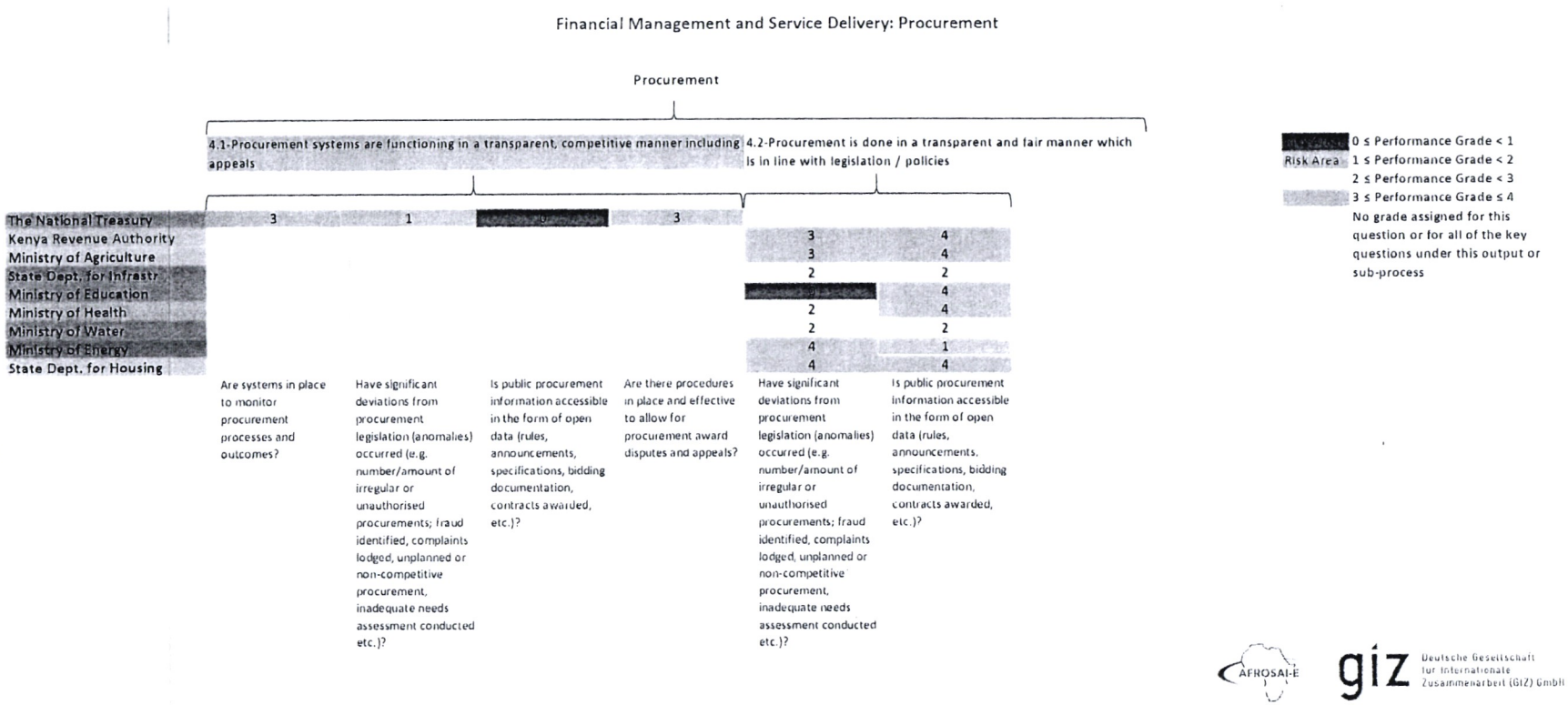
Root Causes of Underperformance
Percent assignment of each Root Cause of Underperformance across all Key Questions for this process (excludes Key Questions with a performance grade of 4 which were not assigned a Root Cause of Underperformance)



Dominant Root Cause of Underperformance by Institution
Identified by auditors considering the root causes identified for all Key Questions under this process

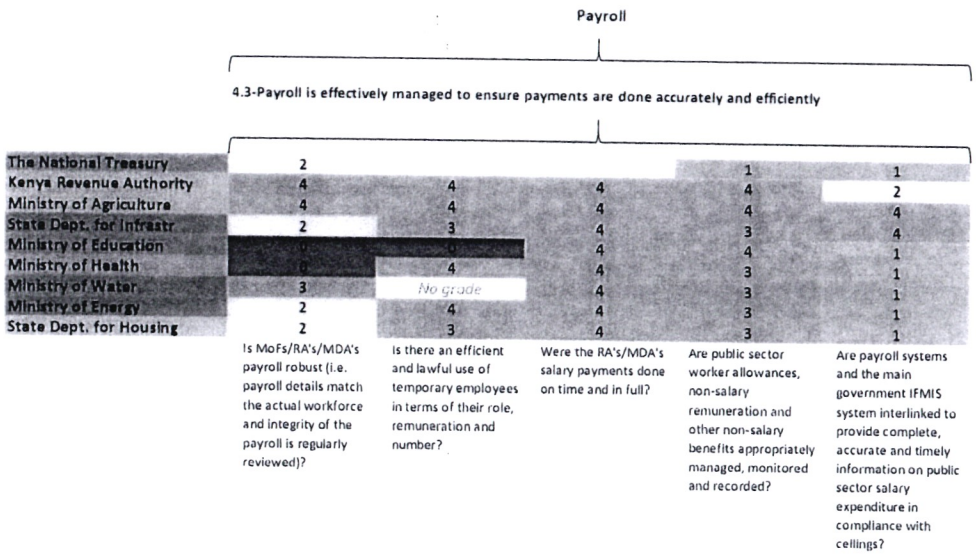
The National Treasury	(4) Governance and oversight
Kenya Revenue Authority	N/A
Ministry of Agriculture	(1) Policy and legal framework
State Dept. for Infrastr	
Ministry of Education	(4) Governance and oversight
Ministry of Health	(4) Governance and oversight
Ministry of Water	(4) Governance and oversight
Ministry of Energy	(4) Governance and oversight
State Dept. for Housing	

Appendix 6: Procurement



Appendix 7: Payroll

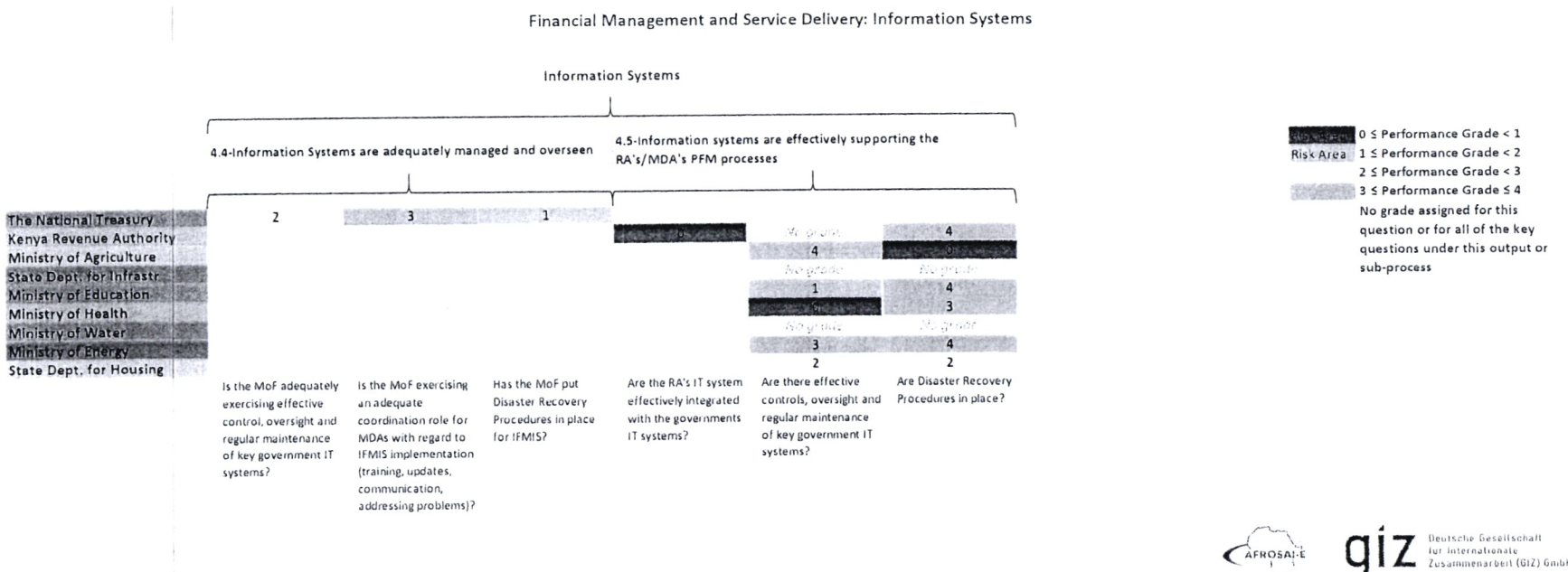
Financial Management and Service Delivery: Payroll



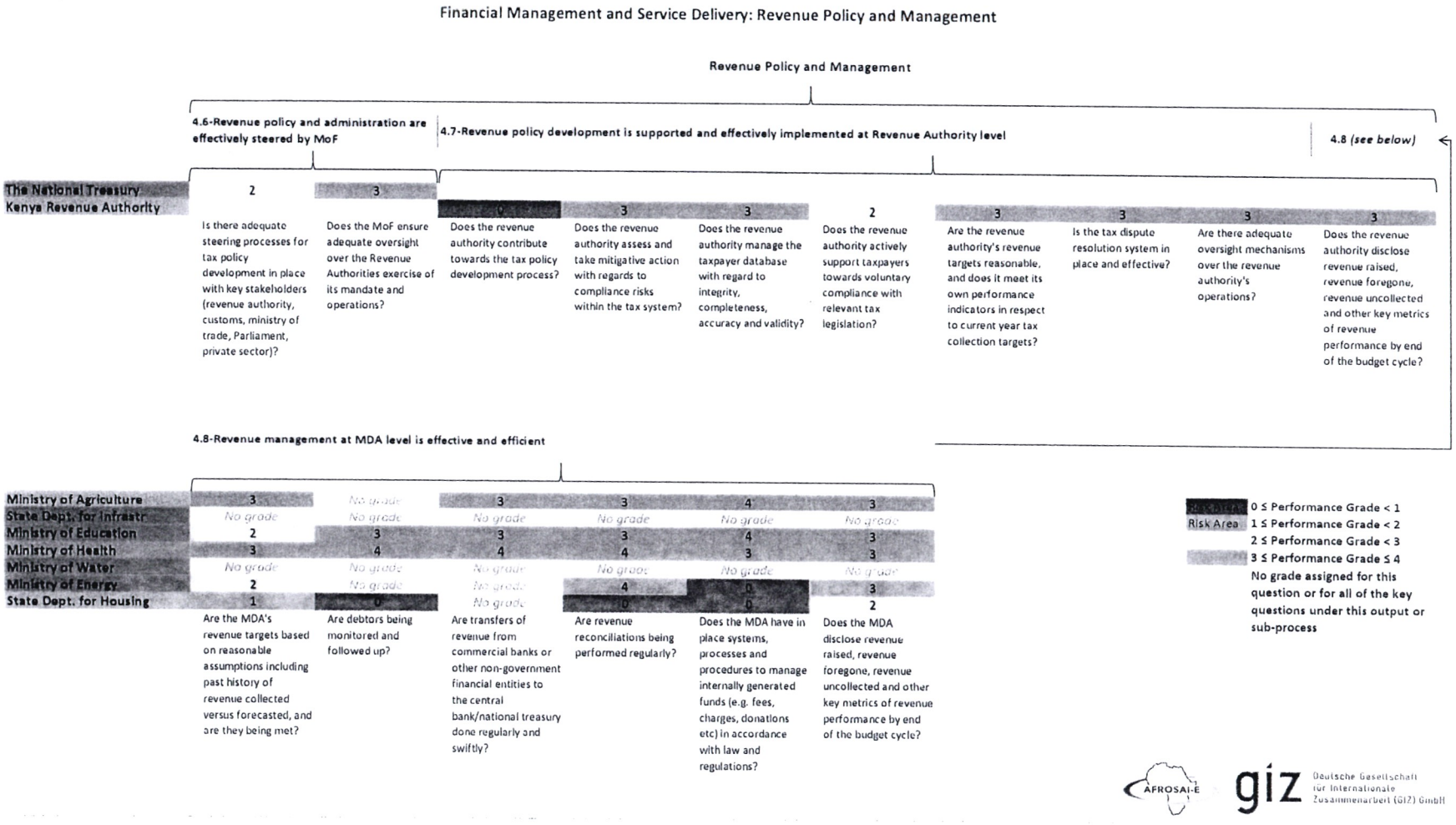
Risk Area

0 ≤ Performance Grade < 1
1 ≤ Performance Grade < 2
2 ≤ Performance Grade < 3
3 ≤ Performance Grade ≤ 4
No grade assigned for this question or for all of the key questions under this output or sub-process

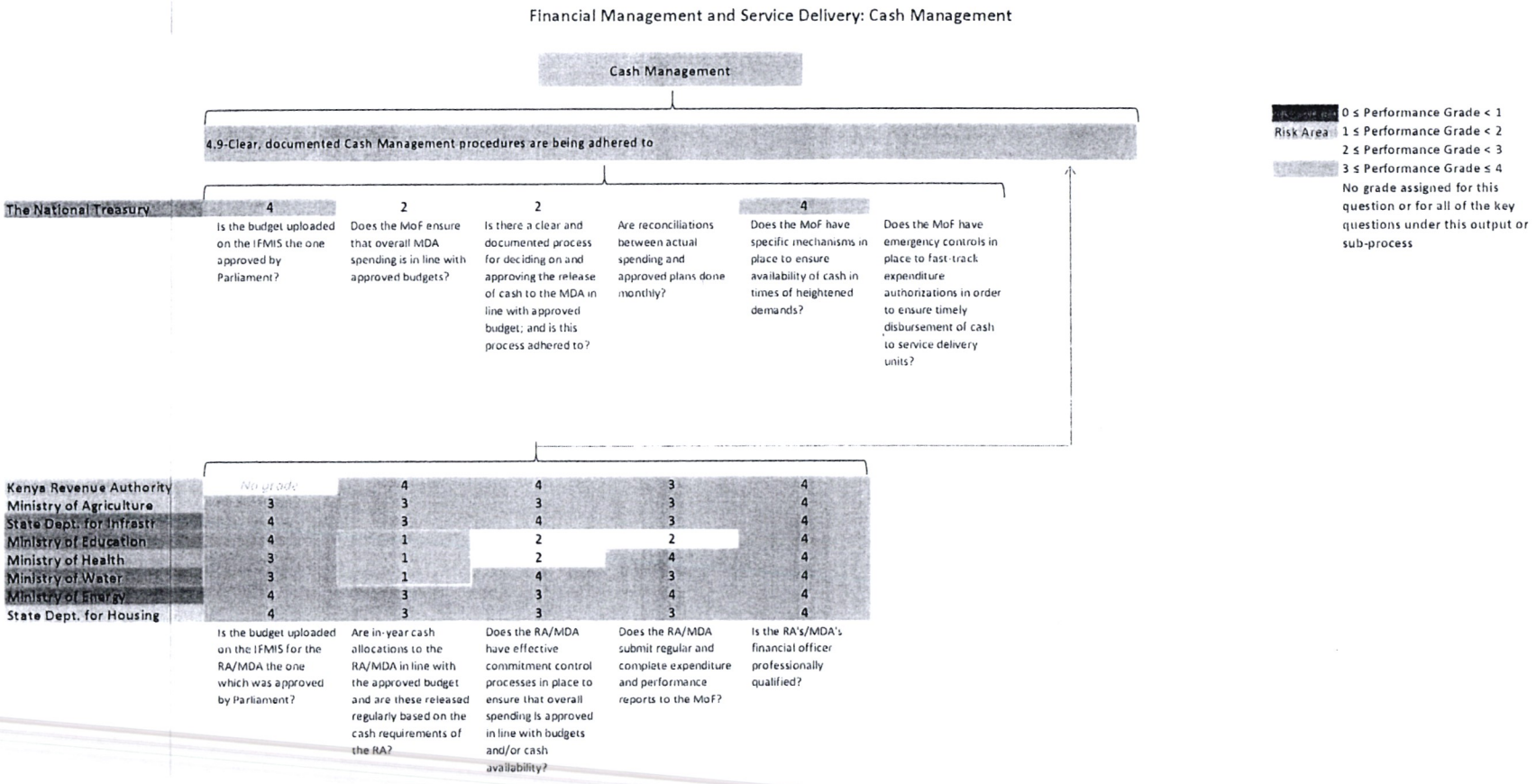
Appendix 8: Information Systems



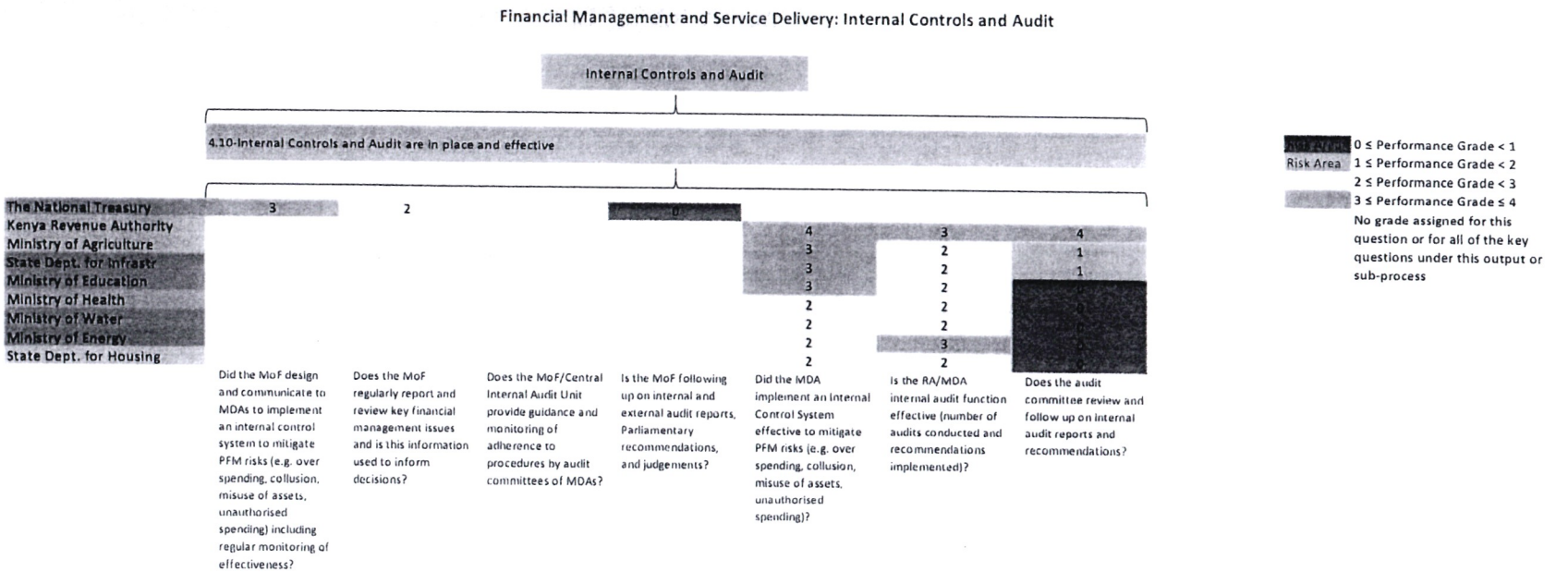
Appendix 9: Revenue Policy and Management



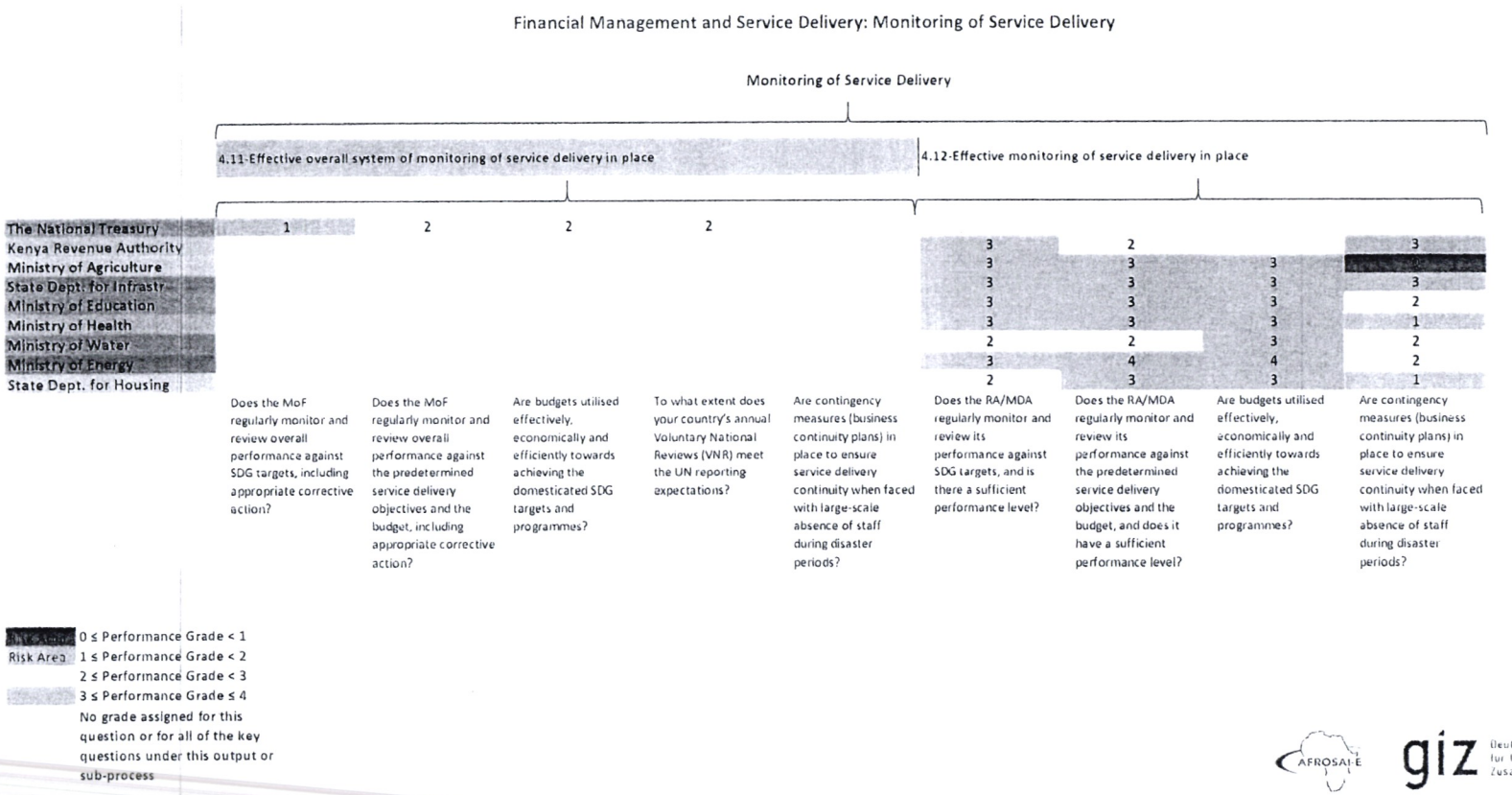
Appendix 10: Cash Management



Appendix 11: Internal Controls and Audit



Appendix 12: Monitoring and Service Delivery



Appendix 13: Performance: Accounting, Reporting and Oversight

Performance: Accounting, Reporting and Oversight

Overall Process Performance
Average of the performance of all the institutions engaged in this process

3.2

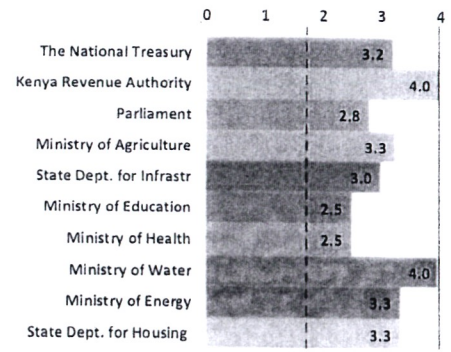
Key Risk Area?
Risk Area if the performance grade is less than 2

No

Quality Assessment
Number and percent of Key Questions with response of "Not applicable"

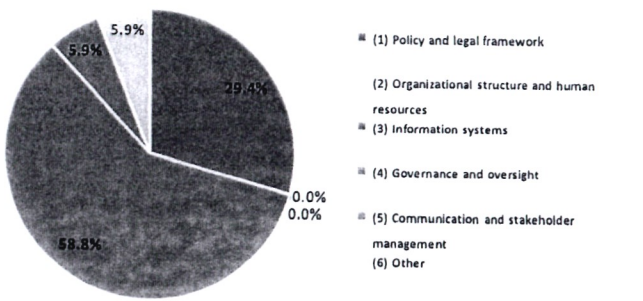
Not applicable		All others		Total questions
3	7.1%	39	92.9%	42

Performance by Institution
Average of all Key Questions assessed for this process for each institution



Risk area below this line
Target performance grade

Root Causes of Underperformance
Percent assignment of each Root Cause of Underperformance across all Key Questions for this process (excludes Key Questions with a performance grade of 4 which were not assigned a Root Cause of Underperformance)



Dominant Root Cause of Underperformance by Institution
Identified by auditors considering the root causes identified for all Key Questions under this process

The National Treasury	
Kenya Revenue Authority	N/A
Parliament	(4) Governance and oversight
Ministry of Agriculture	(4) Governance and oversight
State Dept. for Infrastr	
Ministry of Education	(4) Governance and oversight
Ministry of Health	(1) Policy and legal framework
Ministry of Water	N/A
Ministry of Energy	(6) Other
State Dept. for Housing	

National Assembly- OAG Reports 2020 Volume 20

1. NACADA Bi annual Report on the Status of Alcohol and drug Abuse control in Kenya .Paper Laid 10/3/2020
2. Quarterly economic and Budgetary Review third Quarter Financial Year 2019/2020.paper Laid 2/7/2020
3. Kenya Bankers Association Annual Report and Financial Statement. Paper Laid 5/8/2020
4. Performance Audit Report on Installation and Maintenance of Road Furniture. Paper Laid 22/12/2020
5. Performance Audit Report on Land Conservation and Restoration of Quarries in Kenya. Paper Laid 6/10/2020
6. Performance Audit Report on Fire safety preparation in schools. Paper Laid 6/10/2020
7. Special Report on Performance of the Public Finance Management System for the Year 2019-2020.paper laid 16/2/2020
8. Special Audit Report of the auditor general on Accounts of the National Land commission(payment on behalf of other Government Entities).Paper Laid 8/9/2020
9. Report of the Auditor-general on the Financial statement for National Government for the 2016/2017